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IN THE

Supreme Court of the United States

OCTOBER TERM, 1986

SOUTHERN UNION COMPANY,
UNICON PRODUCING COMPANY,
SOUTHLAND ROYALTY COMPANY and
EXXON CORPORATION,
Petitioners,

v.

JICARILLA APACHE TRIBE,
DONALD P. HODEL, Secretary of the
United States Department of the Interior,
and STATE OF NEW MEXICO,
Respondents.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

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QUESTIONS PRESENTED

In *Nevada v. United States*, 463 U.S. 110, 144 n.16 (1983), this Court stated, "If in carrying out their role as representative, the Government violated its obligations to the Tribe, then the Tribe's remedy is against the Government, not against third parties."

The questions presented by this petition are:

(a) Whether the Federal Government violates its obligation to an Indian tribe when it determines royalties under oil and gas leases issued pursuant to the Indian Mineral Leasing Act of 1938 through an exercise of discretion as expressly authorized by federal law and regulation; and

(b) Whether, even if it does so, the Tribe's remedy for such violation is against third parties who do not participate in the Government's breach of trust but instead rely upon the Government's determination of royalties under federal law and regulation.

LIST OF PARTIES

The caption contains the names of all parties to the proceedings before the United States Court of Appeals for the Tenth Circuit.

Petitioner, Southern Union Company, is a corporation organized under the laws of the State of Delaware, whose principal place of business is Dallas, Texas. Southern Union Company has no parent corporation and no subsidiaries or affiliates other than wholly-owned subsidiaries.

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JICARILLA APACHE TRIBE,
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Respondents.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

Petitioner, Southern Union Company, respectfully prays that a Writ of Certiorari issue to review the *en banc* judgment and opinion of the United States Court of Appeals for the Tenth Circuit, entered in this proceeding on January 23, 1986, reported at 782 F.2d 855 (10th Cir. 1986), supplemented on June 18, 1986, reported at 793 F.2d 1171 (10th Cir. 1986).

OPINIONS BELOW

The United States Court of Appeals for the Tenth Circuit on rehearing en banc rendered its decision on January 23, 1986. The decision is reported at 782 F.2d 855 (10th Cir. 1986) and is reprinted in the Petitioners' Joint Appendix ("Jt. App.") at Jt. App. 1a. Petitioners' Joint Appendix is filed concurrently herewith on behalf of the Petitioners, Southern Union Company, Unicon

Producing Company, Southland Royalty Company and Exxon Corporation. The Court of Appeals supplemented its *en banc* decision on June 18, 1986. The supplemental decision is reported at 793 F.2d 1171 (10th Cir. 1986) and is reprinted at Jt. App. 18a. The decision of the three-judge panel of the Court of Appeals, which first heard this appeal, was rendered February 24, 1984. The panel decision is reported at 728 F.2d 1555 (10th Cir. 1984) and is reprinted at Jt. App. 21a. The opinion and order of the United States District Court for the District of New Mexico following the trial on the merits was entered November 5, 1979. The decision is reported at 479 F. Supp. 536 (D.N.M. 1979) and is reprinted at Jt. App. 104a.

In addition, the following opinions and orders of the District Court are reprinted in the Petitioners' Joint Appendix: (a) Opinion and Order of the United States District Court for the District of New Mexico on cross-motions for partial summary judgment, filed September 7, 1978, at Jt. App. 66a and 73a; (b) Opinion and Order of the United States District Court for the District of New Mexico denying plaintiff's motion to reconsider partial summary judgment, filed December 19, 1978, at Jt. App. 75a; (3) Opinion and Order of the United States District Court for the District of New Mexico denying defendants' motion to dismiss plaintiff's second amended complaint, filed April 13, 1979, at Jt. App. 79a and 102a; (d) Opinion and Order of the United States District Court for the District of New Mexico pertaining to accounting of royalties on oil and gas leases, filed July 30, 1980, at Jt. App. 141a; (e) Order of the United States District Court for the District of New Mexico on motions to reconsider the July 30, 1980 opinion and order, filed January 26, 1981, at Jt. App. 154a; (f) Opinion and Order of the United States District Court for the District of New Mexico on cross-claims of Southland Royalty Company, Supron Energy Corporation and Exxon Corporation against Gas Company of New Mexico, filed June 1, 1981, at Jt. App. 165a and 173a; and (g) Order

of the United States District Court for the District of New Mexico amending order of June 1, 1981, filed July 1, 1981, at Jt. App. 175a.

The opinion of the United States Department of the Interior, Interior Board of Land Appeals, on consolidated appeals from decisions of the Acting Deputy Commissioner for Indian Affairs pertaining to royalty values, decided March 21, 1980, is reported at 46 I.B.L.A. 181 (1980) and is reprinted at Jt. App. 176a.

JURISDICTION

The Respondent, Jicarilla Apache Tribe, originally filed this suit in the United States District Court for the District of New Mexico on May 7, 1975. After amendment of its complaint and further amendment to allow the pleadings to conform to the proof at trial, the Tribe invoked federal jurisdiction under 28 U.S.C. §§ 1331, 1332 and 1362 (1982); 25 U.S.C. §§ 396a-g (1982); 5 U.S.C. §§ 701-706 (1982); and 15 U.S.C. §§ 1, 2, 15 and 19 (1982). Following trial on the merits, the District Court rendered its decision on November 5, 1979. After entry of supplemental interim opinions and orders, the District Court entered final judgment on June 1, 1981. All parties filed timely notices of appeal and cross-appeal to the United States Court of Appeals for the Tenth Circuit.

On February 24, 1984, a divided three-judge panel of the United States Court of Appeals for the Tenth Circuit affirmed in part and reversed in part the judgment of the District Court. On January 26, 1986, on rehearing, a divided Court of Appeals for the Tenth Circuit sitting *en banc* affirmed in part and reversed in part the judgment of the District Court and adopted the prior dissenting opinion to the panel decision, with certain exceptions and additions, as the opinion of the Court. Petitioners Southern Union Company, Unicon Producing Company and Exxon Corporation timely filed petitions for further rehearing with suggestion for rehearing *en banc* on February 5 and 6, 1986. The Court of Appeals denied the

petitions for rehearing on April 15, 1986. Following the granting of an extension of time, the Secretary of the Interior timely filed an application for modification of the Court's *en banc* decision on March 6, 1986. The Court denied the Government's application for modification of its *en banc* opinion on June 18, 1986. On that same date, the Court of Appeals, on its own motion, issued a supplement to the *en banc* opinion.

Upon the filing of timely applications with this Court, the Honorable Byron R. White granted Petitioners Southern Union Company, Unicon Producing Company, Southland Royalty Company, and Exxon Corporation extensions of time to and including August 13, 1986 within which to file petitions for writ of certiorari. The jurisdiction of this Court to review the *en banc* Opinion of United States Court of Appeals for the Tenth Circuit, filed January 23, 1986 and supplemented June 18, 1986, is invoked under 28 U.S.C. § 1254(1) (1982).

STATUTES AND REGULATIONS INVOLVED

25 U.S.C. § 396a-g (1982), Indian Mineral Leasing Act of 1938. The full text of the Indian Mineral Leasing Act is reprinted at Jt. App. 200a.

25 C.F.R. Part 211 (1985) (formerly codified at 25 C.F.R. Part 171 (1981)), reprinted at Jt. App. 214a.

30 C.F.R. Part 221 (1981), reprinted at Jt. App. 238a.

30 C.F.R. Part 206 (1985), reprinted at Jt. App. 283a.

43 C.F.R. Part 3160 (1985), reprinted at Jt. App. 291a.

STATEMENT OF THE CASE

Introduction

This petition concerns the liability of three natural gas producers [1] to the Jicarilla Apache Tribe ("the Tribe")

[1] The three producing companies are Unicon Producing Company ("Unicon"), formerly Supron Energy Corp. ("Supron"), formerly Southern Union Production Company ("SUPC"); Southland Roy-

for the alleged underpayment of royalties from 1970 to the present. The royalties are derived from the value of natural gas produced on reservation land. All sixteen reservation oil and gas leases in question ("the IMLA Leases") have been issued since 1950 pursuant to the Indian Mineral Leasing Act of 1938 ("IMLA"), 25 U.S.C. § 396a-g (1982). Under the IMLA, all lease operations, including the determination of royalties, are "subject to the rules and regulations promulgated by the Secretary of the Interior [("the Secretary")]." 25 U.S.C. § 396d. From the time the IMLA Leases were first entered into until the filing of this action, the Secretary exercised his discretion as expressly provided by the regulations to determine the Tribe's royalties based on the sales price of the gas. The Tribe sought to impose upon the Secretary different royalty accounting procedures under the regulations. The Tribe prevailed. Thus, the purported underpayment of royalties is the result of the Lessees' faultless compliance with the Secretary's interpretation of his own regulations in the exercise of his discretion, which the District Court and the Court of Appeals held violated the Federal Government's fiduciary duty to the Tribe.

I. THE FACTUAL SETTING

A. The Production and Sale of Natural Gas Under the IMLA Leases and the Extraction of Liquid By-Products

All of the gas produced under the IMLA Leases contains liquid hydrocarbon substances, such as butane, propane and natural gasoline. Their presence increases the Btu content of the gas. Because of its relatively high liquid content, the gas involved in this case is called "wet gas."

All of the gas produced under the IMLA Leases was sold at the wellhead by the Lessees to Southern Union

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alty Company ("Southland"), formerly Aztec Oil and Gas Co. ("Aztec"); and Exxon Corporation ("Exxon"); hereinafter collectively "the Lessees."

Company ("Southern Union," formerly Southern Union Gas Company), for use by its operating division, Gas Company of New Mexico ("GCNM"), New Mexico's largest natural gas public utility.[2] The gas purchase agreements pertaining to the IMLA Leases date from 1953. Originally, Southern Union paid a base contract price for natural gas produced from the IMLA Leases. As the market for liquid by-products developed, Southern Union began to pay the Lessees a base price plus a penny per thousand cubic feet of gas for the liquid content. Beginning in 1974, the gas sales contracts included a pricing provision by which the contract price was adjusted to reflect the actual Btu content of the gas. The Btu price adjustment increased the amount realized by the Lessees upon sale of the gas and accounted for the value of the liquid components.

Following purchase at the wellhead, Southern Union transported the gas through its pipeline system to its processing plant. There, the wet gas was separated into its constituent liquid by-products and residue dry gas. From 1971 to 1976 the processing plant was owned and operated by SUPC, in which Southern Union then held a controlling interest. Following extraction at the plant, the liquid products were sold to third parties. During the period SUPC owned the plant, it received a portion of the revenues derived from sale of the liquids. Southern Union always retained ownership of the residue dry gas, which was sold after the completion of processing to customers of GCNM.

Under the gas sales contracts, Southern Union received title to the wet gas at the wellhead and had the right to extract all liquid by-products. With the exception of SUPC during the period it owned the processing plant,

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[2] On January 28, 1985 Southern Union sold substantially all of the assets of GCNM to Public Service Company of New Mexico. As part of that sale Southern Union retained certain liabilities, including liability up to the date of sale for additional royalties which may be assessed in this litigation.

none of the Lessees ever derived any revenue from the extraction and sale of liquids. The actual amount realized by the Lessees from the sale of the wet gas produced under the IMLA Leases was the Btu-adjusted sales price.

B. The Secretary's Determination of the Tribe's Royalties

The IMLA Leases are all standard-form federal lease agreements.[3] With respect to the computation of royalties, the IMLA Leases provide that royalties shall be based on the value of the gas. In this regard, Paragraph 3(c) of the IMLA Leases tracks the language in 25 C.F.R. § 211.13(a) (1985), which provides in part as follows:

> . . ."[V]alue" for the purposes of the lease may, in the discretion of the Secretary of the Interior, be calculated on the basis of the highest price paid or offered (whether calculated on the basis of short or actual volume) at the time of production for the major portion of the oil of the same gravity, and gas, and/or natural gasoline, and/or all other hydrocarbon substances produced and sold from the field where the leased lands are situated, and the actual volume of the marketable product less the content of foreign substances as determined by the supervisor. *The actual amount realized by the lessee from the sale of said products may, in the discretion of the Secretary of the Interior, be deemed mere evidence of or conclusive evidence of such value.*

25 C.F.R. § 211.13(a) (1985) (emphasis added).[4]

Paragraph 3(g) of the IMLA Leases also incorporates additional federal regulations which deal with royalty de-

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[3] U.S. Dept. of Interior, Oil and Gas Mining Lease for Tribal Indian Lands, Lease Form 5-157 (1964). The lease form has remained essentially unchanged since 1939 and is reproduced at Jt. App. 377a.

[4] This regulation was formerly codified at 25 C.F.R. § 171.13(a) (1981); it was redesignated March 30, 1982.

termination.[5] These regulations gave the Secretary complete authority to determine the Tribe's royalties. The Secretary had authority to approve, modify or revoke all gas sales contracts. The Secretary prohibited lessees from selling natural gas without a sales contract first approved by him. The Secretary established the value of the gas for royalty purposes. The Secretary rendered monthly statements for the amount accruing as royalty from each lease. And the Secretary required all lessees to tender payment of royalties in accordance with the value he determined.[6]

The Lessees paid royalties based upon such determinations by the Secretary. Each month the Secretary required the Lessees to file a report showing all sales of gas from the IMLA Leases and the resulting royalty accruing to the Tribe.[7] The Secretary required the Lessees to verify in this report the volumes of gas produced and its sales price and to compute the value of the gas for royalty purposes by multiplying the volume of production times the sales price. Transcript ("Tr.") Vol. I at 155-156. With this "standard method" of reporting royalties, the Secretary also required the Lessees to file a monthly remittance form, accompanied by payment of the Tribe's royalties.[8] Thereafter, the Secretary reviewed

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[5] Paragraph 3(g) incorporates the regulations found in 30 C.F.R. Part 221 (1981), which were amended and redesignated effective November 26, 1982. Prior to that date these regulations had remained essentially unchanged since first promulgated in 1942. *See* 7 Fed. Reg. 4132 (1942). The provisions governing oil and gas lease operations, other than royalty accounting, are now codified in 43 C.F.R. Part 3160 (1985). The regulations which concern royalty determination are codified in 30 C.F.R. Part 206 (1985). The prior regulations are cited in this petition where there is no corresponding provision in the new regulations or where the new regulations are different from the regulations in effect at the time of the Secretary's actions in this case.

[6] *See*, respectively, 30 C.F.R. §§ 221.3, 221.12, 221.13, 221.38, 221.40 and 221.47 (1981).

[7] *Id.* § 221.62; Form 9-361, reproduced at Jt. App. 387a.

[8] *Id.* § 221.63.

these reports and issued his statement of account with respect to each lease.[9] Until this litigation, the Secretary uniformly followed this procedure to bill and collect the Tribe's royalties. In short, the Secretary exercised his discretion to accept the actual amount realized by the Lessees from the sale of the gas as conclusive evidence of its royalty value.

II. PROCEEDINGS IN THE COURTS BELOW

A. The Tribe Sues for Additional Royalties Based on Dual Accounting.

Dissatisfied with the royalty income derived from the Secretary's determination of value, the Tribe initiated this action in 1975, claiming jurisdiction under 28 U.S.C. §§ 1331, 1332, 1362 (1982); 25 U.S.C. § 396a-g (1982); and 5 U.S.C. §§ 701-706 (1982). The Tribe alleged that under the IMLA Leases and the regulations the Secretary was required to determine the royalty value of wet gas in two distinct ways and to compute its royalties by using the higher value. In such "dual value accounting," the sales price of the gas at the wellhead is compared to the aggregate value of the liquid by-products extracted from the gas plus the value of the residue dry gas less an allowance for the cost of extraction.[10] *See* 30 C.F.R. §§ 206.105(c), 206.106 (1985). Royalty computations are then based on the higher of these two amounts.

The Tribe drew support for its dual accounting claim from the last sentence in Paragraph 3(c) of the IMLA Leases and the corresponding sentence in 25 C.F.R. § 211.13(a) (1985), which provides:

> In determining the value for royalty purposes of products, such as natural gasoline, that are derived from treatment of gas, a reasonable allowance for

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[9] *Id.* §§ 221.12, 221.40.

[10] "Aggregate value" royalty accounting is commonly known as "net realization" accounting. The two terms are used interchangeably. Net realization means the value of the extracted liquid by-products and residue dry gas, after allowance for the cost of manufacture.

> the cost of manufacture shall be made, such allowance to be two-thirds of the value of the marketable product unless otherwise determined by the Secretary of the Interior on application of the lessee or on his own initiative, and that *royalty will be computed on the value of gas or casing-head gas, or on the products thereof (such as residue gas, natural gasoline, propane, butane, etc.), whichever is the greater.*

25 C.F.R. § 211.13(a) (1985) (emphasis added).

The Tribe argued that this sentence mandated dual value accounting by the Secretary. Dual accounting was not a new concept in the computation of royalties under leases subject to federal regulation. The Secretary had required dual accounting by lessees who, instead of selling wet gas at the wellhead, elected to process the gas, either themselves or through an affiliate, and to sell the extracted liquid products and residue dry gas after processing. The Secretary required SUPC, for example, to provide dual accounting for the Tribe's royalties when it owned and operated the processing plant. Tr. Vol. I at 122; Tr. Vol. II at 36-37. *See In re Supron Energy Corp.*, 46 I.B.L.A. 181 (1980), Jt. App. 176a. The Secretary's dual accounting practice thus appeared consistent with the applicable regulation which provides:

> If the lessee derives revenue on gas from two or more products, a royalty normally will be collected on all such products.

30 C.F.R. § 206.105(b) (1985). Moreover, as of the time of trial the Secretary had never required dual value accounting by any lessee who did not own an interest in a processing plant or otherwise profit from the extraction and sale of liquid products. Tr. Vol. I at 126, 138; Tr. Vol. II at 34; *see also* Jt. App. 24a.

According to the Tribe, however, the failure of the Secretary to require dual accounting by all Lessees for its royalties constituted a breach of the Federal Government's fiduciary duty. As for the Lessees, the Tribe alleged that their failure to pay royalties based on the higher of the two values that would have been derived

through dual accounting constituted breach of the IMLA Leases, regardless of the failure of the Secretary to require them to so account.

B. The District Court Rejects Dual Accounting, Then Reverses Itself.

Initially, the District Court rejected the Tribe's dual accounting claim. The court held on summary judgment that the Secretary's determination of the Tribe's royalties:

> [W]as an exercise of the Secretary's discretion based upon the regulations and the leases, whereby he conclusively established value for royalty purposes as the sale price received at the wellhead.

Jt. App. 68a. The Tribe moved for reconsideration. The court denied the motion and remarked:

> Sales price may be taken by the Secretary to be conclusive evidence of value for royalty purposes. . . . His action in doing so does not constitute an abuse of this discretion.

Jt. App. 76a (citations omitted).

Despite these rulings, the District Court revived the Tribe's dual accounting claim after trial on the merits. Without reference to any substantive legal source, the court held that the Secretary had breached a fiduciary duty to the Tribe "because the method by which he computed royalties did not derive for the Tribe the highest royalties payable under the lease terms and the federal regulations. . . ." Jt. App. 126a. The court ordered the Secretary to require dual accounting by all Lessees. Jt. App. 135a.

The court reasoned that, because the Federal Government had breached its fiduciary duty to the Tribe by failing to require dual value accounting, the Lessees necessarily had breached the IMLA Leases with respect to the payment of royalties, although their breaches were "technical in nature," Jt. App. 136a, and occurred "through no apparent fault" of their own, Jt. App. 127a. The court ordered the Lessees to account prospectively for

tribal royalties in accordance with the dual accounting procedures it imposed on the Secretary, Jt. App. 139a, and, without any reference to the law of fiduciary responsibility, it awarded retrospective damages to the Tribe against the Lessees for the amount by which the Tribe's royalties purportedly had been underpaid from 1970 until the court's decision in 1979.[11] Jt. App. 138a, 139a.

C. The Court of Appeals Expressly Rejects the Imposition of Fiduciary Standards, Then Reverses Itself.

A divided panel of the Court of Appeals reversed the District Court's judgment requiring dual value accounting. The majority expressly recognized that the Secretary may exercise discretion to determine the Tribe's royalties based on the sales price of the gas. Jt. App. 26a. The majority found nothing in the record to indicate that the Secretary had acted arbitrarily or capriciously by not requiring dual accounting by all Lessees. Jt. App. 29a. The majority found that the Secretary's royalty accounting practices had a reasonable basis in the lease and the regulations, conformed to standard royalty accounting practices in the oil and gas industry, and were consistent with case law in the Tenth Circuit. Jt. App. 28a-29a. Thus, the majority concluded there was "no basis for the trial court's determination as to fiduciary standards." Jt. App. 30a.

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[11] When the Tribe sued the Lessees for additional royalties, the Lessees filed crossclaims against Southern Union for indemnification. The indemnity claims were based on an "excess royalty" clause in the gas sales contracts, which provided that if royalty payments to the Tribe were calculated on a value in excess of the sales price of the gas, Southern Union would reimburse the Lessees for such additional amounts. When the District Court entered judgment against the Lessees, it also entered judgment against Southern Union on the crossclaims. The Court of Appeals affirmed both judgments. Southern Union, by this petition, seeks review of the judgment against the Lessees and of the judgment against it on the crossclaims.

On rehearing, a divided Court of Appeals sitting *en banc* overruled the majority and adopted the dissenting opinion to the panel decision. Jt. App. 3a. The court held that the Federal Government had breached its fiduciary obligation to the Tribe by failing to require dual accounting by all Lessees for the Tribe's royalties. Jt. App. 48a. The court decided that the IMLA created an express trust between the Government and the Tribe with respect to the determination of its royalties. Jt. App. 40a. The court found that the purpose of the IMLA trust is to derive the "greatest return" for the Tribe, Jt. App. 40a, and concluded that the Government's fiduciary duty required the Secretary to apply whichever royalty accounting method authorized by the regulations yields the Tribe the "greatest royalties." Jt. App. 48a. Like the District Court, the Court of Appeals made no reference to the law of fiduciary responsibility in affirming the judgment in favor of the Tribe and against the Lessees.

D. The Court of Appeals Imposes Liability Against the Lessees for the Federal Government's Breach of Trust to the Tribe.

In a supplement to the *en banc* opinion, the court for the first time addressed the question who must pay for the United States' purported breach of trust to the Tribe. Calling attention to the statement of this Court in *Nevada v. United States*, 463 U.S. 110, 144 n.16 (1983), the Lessees and Southern Union had argued that the Tribe's remedy for breach of a fiduciary obligation by the Government is against the Government, not against them. The court rejected this argument. Reasoning that the relationship between the Tribe and the Lessees is contractual, the court held:

> That the Secretary breached its fiduciary duty to properly enforce the leases does not excuse the lessees from subsequently having to pay the amounts determined to be owed under the leases.

Jt. App. 19a.

E. The Federal Government Seeks to Impose Liability on the Lessees, While Maintaining That It Has Never Breached Its Obligation to the Tribe.

Throughout this litigation the Federal Government has attempted to uphold the imposition of liability against the Lessees for the damages caused by the Secretary's alleged violation of his obligation to the Tribe. Despite being found liable for breach of trust, the Government did not appeal the District Court's ruling, ordering the Secretary to require dual accounting by all Lessees in determining the Tribe's royalties. Before the three-judge panel the Government argued that the trial court's dual accounting order should not be disturbed because the Secretary has the discretion under the regulations to require dual value accounting by all Lessees and desired to do so, retroactively as well as prospectively.[12] The panel majority found, however, that the Secretary had changed his position respecting dual accounting in response to rulings by the District Court. Jt. App. 29a. The majority ruled that the Secretary's prior long-standing dual accounting procedures must be applied through the conclusion of this case. *Id.*

On rehearing the Government made a different argument. It asserted that prior to the District Court's decision the Secretary had already decided to require dual accounting by all Lessees for the Tribe's royalties. This independent exercise of administrative discretion is purportedly embodied in a statement in a trial court brief filed in other litigation in which the Secretary apparently indicated that dual accounting by all lessees would be implemented "if the authority to do so is clarified." [13]

Disturbed by the *en banc* decision holding that the Secretary in fact had breached his obligation to the

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[12] Secretary of the Interior, Reply Brief, *Jicarilla Apache Tribe v. Supron Energy Corp.*, No. 81-1860 at 5-8 (10th Cir.).

[13] *See* Secretary of the Interior, Supplemental Brief on Rehearing, *Jicarilla Apache Tribe v. Supron Energy Corp.*, No. 81-1860 at 12-14 (10th Cir.).

Tribe, the Government sought to revise the court's opinion. In its application to modify the standard of liability for breach of trust adopted by the Court of Appeals, the Government argued for a third time that the Lessees should pay for the harm caused by the Secretary's breach. According to the Federal Government, the imposition of damages against the Lessees in favor of the Tribe serves merely to return the parties "to the position they should have occupied all along." [14]

Despite these attempts to shift liability to the Lessees for its actions, the Government also has maintained consistently that the Secretary has never breached any obligation of trust to the Tribe. Indeed, before the three-judge panel the Government argued that the IMLA does not establish fiduciary duties in the Secretary's administration of the IMLA Leases.[15] And, when the Government moved to modify the court's *en banc* decision, it asserted that the "opinion articulates the judicial standard for finding a breach of fiduciary duty by the Secretary in a way that is in conflict with both the case law developed in the Court of Claims . . . and the understanding of Congress." [16] The Government contended that the standard by which to test the liability of the Secretary for breach of Indian trust obligations is "whether the Secretary's actions were 'in good faith and within the realm of their acceptable [discretion], or were they arbitrary, capricious, an abuse of discretion, or contrary to law?' " [17] The Government urged the court to revise the *en banc* opinion to prevent an "erroneous 'split in the circuits' concerning the proper standard for judicial resolution of

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[14] Secretary of the Interior, Application for Modification of the Court's *en banc* Decision, *Jicarilla Apache Tribe v. Supron Energy Corp.*, at 4 n.2 (10th Cir.).

[15] Secretary of the Interior, Brief-in-Chief, *Jicarilla Apache Tribe v. Supron Energy Corp.*, No. 81-1860 at 19-22 (10th Cir.).

[16] Secretary of the Interior, Application for Modification, *supra* n.14 at 6 (citations omitted).

[17] *Id.* (citations omitted).

breach of fiduciary duty claims." [18] The Court of Appeals denied the motion. Jt. App. 18a.

The liability of the Lessees for the Government's alleged violation of a fiduciary obligation to the Tribe having been affirmed, this Petition for Writ of Certiorari has followed.

REASONS FOR GRANTING THE WRIT

I. THE COURT OF APPEALS ERRONEOUSLY IMPOSED LIABILITY ON INNOCENT THIRD PARTIES FOR THE FEDERAL GOVERNMENT'S PURPORTED BREACH OF TRUST.

"[I]f it were held that there was a breach of duty by the Secretary the trial court applied the remedy to the wrong parties and so punished the lessees although it stated that they were in no way at fault." Jicarilla Apache Tribe v. Supron Energy Corp., 782 F.2d 855, 861 (10th Cir. 1986) (Seth, C.J., dissenting).

A. The Decision Below Conflicts With *Nevada v. United States, United States v. Mitchell* and *Seminole Nation v. United States.*

In a four-to-three *en banc* decision, the Court of Appeals has created a unique remedy in federal Indian law. According to the court, an Indian tribe has a remedy against innocent third parties for the harm caused by the Government's breach of trust. This remedy is unknown to the law of fiduciary relations. And its use conflicts with specific principles articulated by this Court.

In *Nevada v. United States*, 463 U.S. 110 (1983), this Court held that a judicial decree, adopted pursuant to a settlement agreement entered into by the United States on behalf of an Indian tribe adjudicating the tribe's water rights, precluded the tribe from bringing a subsequent action for additional water rights against other parties bound by the same settlement. Although *Nevada* was decided under the doctrine of *res judicata*, the principles of

[18] *Id.* at 7.

Indian trust law which the Court there delineated respecting (a) the remedy of an Indian tribe against the United States and (b) the liability of third parties for breach by the United States of its trust obligations, are directly applicable here.

In *Nevada*, the Pyramid Lake Paiute Tribe contended that by representing the interests of both a federal reclamation project and the Tribe in the earlier adjudication of its water rights, the Government breached its fiduciary obligation of undivided loyalty to the Tribe and deprived the Tribe of a full and fair opportunity to be heard in the first proceeding. Based on this alleged denial of due process, the Tribe concluded that the final decree in the prior action could not extinguish its subsequent claim for additional water rights.

This Court concluded otherwise. This Court rejected the proposition that the Government necessarily violates a fiduciary duty to an Indian tribe simply because it represents other federal interests, as required by Congress, in the same litigation. In reaching this decision, the Court also spelled out two basic principles of Indian trust law.

First, the Court assured the Indians they have a remedy for damages against the Government for breach of its trust obligations:

> If, however, the United States actually causes harm through a breach of its trust obligations the Indians should have a remedy against it. I join the Court's opinion on the understanding that it reaffirms that the Pyramid Lake Paiute Tribe has a remedy against the United States for the breach of duty that the United States has admitted.

Id. at 145 (Brennan, J., concurring). Like the Pyramid Lake Paiute Tribe in *Nevada*, the Tribe here also has a remedy against the Government for damages in the Court of Claims. And also like the Tribe in *Nevada*, the Jicarilla Apache Tribe here has taken advantage of that remedy. Jt. App. 41a.

Second, this Court made clear in *Nevada* that the Tribe's remedy is not available against innocent third parties:

> If in carrying out their role as representative, the Government violated its obligations to the Tribe, then the Tribe's remedy is against the Government, not against third parties.

Id. at 144 n.16.

Three days after its declaration of principles in *Nevada*, this Court held in *United States v. Mitchell*, 463 U.S. 206, 226 (1983) (*"Mitchell II"*), that an Indian Tribe has a remedy at law requiring the Federal Government to respond in money damages for breach of fiduciary obligations imposed by federal statutes. Although *Mitchell II* did not address, as this case does, the liability of third parties to the Indian beneficiaries of a federal statutory trust, the decision makes clear that in such situations the United States is held to standards applicable to a private fiduciary. *Id.* The necessary corollary to this rule is that when the Federal Government acts as a private trustee, a third party cannot be held liable for the Government's breach of trust, unless the third party has notice of and participates in the Government's violation of fiduciary duty. *See Restatement (Second) of Trusts* §§ 284, 296, 297 (1959); IV A. Scott, *Law of Trusts* §§ 279A, 283, 296 (3d ed. 1967); G. Bogert, *Law of Trusts and Trustees* §§ 901, 902 (2d ed. rev. 1982).

Moreover, the rule which governs third-party-liability has been applied by this Court to determine the liability of the Government when it has notice of and participates in a trustee's breach of duty. *Seminole Nation v. United States*, 316 U.S. 286 (1942); *cf. United States v. Dann*, 105 S.Ct. 1058, 84 L.Ed.2d 28, 35-36 (1985). In *Seminole Nation*, this Court reviewed whether the United States could be held liable for the misappropriation by tribal fiduciaries of federal funds paid by the Government to the tribe for the benefit of its individual members. This Court recognized that liability could be imposed against the United States because:

> [A] third party who pays money to a fiduciary for the benefit of the beneficiary, with knowledge that the fiduciary intends to misappropriate the money or otherwise be false to his trust, is a participant in the breach of trust and liable therefor to the beneficiary.

Seminole Nation, 316 U.S. at 296 (citations omitted).

Mitchell II described the right of the beneficiary to sue the trustee for damages resulting from breach of trust as "a fundamental incident" of a trust relationship between the United States and an Indian Tribe. *Mitchell II*, 463 U.S. at 226. The decisions in *Seminole Nation*, *Nevada* and *Mitchell II* require the same conclusion here. The well-established principles that determine third-party-liability, and nonliability, for damages resulting from a breach of trust by the trustee must also be a fundamental incident of a trust relationship between the United States and an Indian tribe. Under these decisions, the Tribe's remedy for such damages is properly against the Federal Government, not against the Lessees.

B. The Decision Below Interferes With and Undermines Indian Contracts and the Development of Indian Leasing Enterprises.

If the Court of Appeals' decision is upheld, it will undercut certainty and fairness, the twin goals inherently sought in all commercial transactions, in every agreement between Indians and third parties for which the Federal Government is responsible as trustee.

Other than Indian timber management and management of Indian oil and gas reserves under the IMLA, federal courts have yet to consider what other laws and regulations establish federal fiduciary duties. There are, however, at least seven other statutes that charge the Government with responsibilities in the leasing of Indian land.[19] Thus, the Government plays an important role in

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[19] In addition there are numerous federal statutes which authorize the Federal Government to contract directly with third parties for the purpose of serving a variety of other Indian interests: 25

all leases of Indian land for grazing, mining and farming, as well as for public, religious, educational, recreational, residential and business purposes.[20] In all such leases there is a contractual relationship between the Indians and the lessees, but the Federal Government exercises discretion in supervising the leesees' performance. If the Government's obligation to prescribe and oversee the performance of the lessees is fiduciary in nature then, under the holding of the Court of Appeals, even the Government's breach of "its fiduciary duty to properly enforce the leases does not excuse the lessees from subsequently having to pay the amounts determined to be owed under the leases." Jt. App. 19a.

The grave consequence of this truly aberrant judicial decision is that third parties will no longer be able to engage in Indian commerce on the basis of settled economic expectations. The decision thus jeopardizes the continued development by non-Indians of all Indian natural resources and reservation-based enterprises.

These consequences can perhaps best be understood through an example of how the court's decision would operate in the setting of *Mitchell II*. There, speaking of Indian timber management, this Court observed that "if timber on an allotment has been destroyed through government mismanagement, it will take many years for nature to restore the timber." *Mitchell II*, 463 U.S. at 227-28. For this reason, Congress directed the Secretary, as a trustee, to manage Indian forest resources "on the principle of sustained-yield management." 25 U.S.C. § 466 (1982). To carry out this objective, the Secretary is re-

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U.S.C. § 309 (1982) (adult vocational training); The Johnson-O'Malley Act, 25 U.S.C. §§ 452, 453, 454, 457 (1982) (medical care and social welfare); 25 U.S.C. §§ 458(a)-(g), 458a-e (1982) (school construction); Indian Health Care Improvement Act, 25 U.S.C. § 1601, *et seq.* (1982); 25 U.S.C. § 2001 (1982) (BIA education programs).

[20] *See* 25 U.S.C. § 397 (1982); 25 U.S.C. § 398a-e (1982); 25 U.S.C. § 399 (1982); 25 U.S.C. § 400a (1982); 25 U.S.C. 402a (1982); 25 U.S.C. § 403 (1982); 25 U.S.C. §§ 415, 415a-d (1982).

quired to develop a "harvest schedule," 25 C.F.R. § 163.4 (1985), and to restrict "clear-cutting" of Indian forests, *id.* at § 163.5. If the decision of the Tenth Circuit is allowed to stand, however, it is not just the Government but also the timber cutter who will be liable to the Indians once the land is logged off and of little value. Under the ruling of the Tenth Circuit, even strict compliance with the Secretary's harvest schedule and clearing program, as expressly incorporated into a timber cutting contract, approved by the Secretary, will not prevent the imposition of subsequent liability on the logger, if the Secretary fails to discharge properly his fiduciary obligations.[21]

Like the Lessees here, loggers are supervised by the Secretary in the day-to-day performance of their contracts with the Indians. Like the Lessees here, they are required to deal exclusively with, and must therefore be able to rely upon, the Federal Government in the performance of their contractual obligations. Yet, under the ruling of the Tenth Circuit, no matter how pervasive the Government's authority or how comprehensive its responsibilities over a particular lease, contract or other agreement, from now on third parties will deal with the Federal Government at their peril.

II. THE COURT OF APPEALS APPLIED AN ERRONEOUS STANDARD WHEN IT DETERMINED THAT THE FEDERAL GOVERNMENT COMMITTED A BREACH OF TRUST.

> "[*T*]*here was no finding that the Secretary had acted in an arbitrary or capricious manner. . . . This is mentioned because this finding has unusual implications in this case.*" *Jicarilla Apache Tribe v. Supron Energy Corp., 782 F.2d 855, 857 (10th Cir. 1986) (Seth, C.J., dissenting).*

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[21] *See Mitchell v. United States,* 10 Cl.Ct. 63, 65-66 (1986) (detailing the nature and extent of such claims already brought against the Government by the Indians for breach of trust).

A. The Decision Below Conflicts With *United States v. Mason, United States v. Mitchell* and Decisions Of The Court of Claims.

As announced by the Court of Appeals, when the Government acts as a trustee, the standard of conduct that it must observe is not defined in the terms of the statute and the regulations which establish the Government's trust responsibilities, nor is the standard found in the concept of discretion as that term is used in the law of trusts. The decision therefore conflicts openly with the decisions of this Court in *Mitchell II* and *United States v. Mason*, 412 U.S. 391 (1973).

When the Federal Government has legal as opposed to moral trust obligations to the Indians, it may be held to standards of conduct expected of a private trustee.[22] In *Mason* this Court ruled that when the Government holds Indian money or property in trust pursuant to a federal statute, the Government is bound by such standards. *Id.* at 398. Quoting from Professor Scott's treatise, this Court defined the standard to which the Government must adhere in such situations in familiar terms:

> A trustee is under a duty in administering the trust to exercise such care and skill as a man of ordinary prudence would exercise in dealing with his own property.

Id.[23] Similarly, in *Mitchell II* this Court relied on common-law trust principles to find that the Federal Govern-

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[22] Caution should be used, however, in holding the United States to the same standards required of a private fiduciary. *See Nevada*, 463 U.S. at 142; *see also* Jt. App. 6a.

[23] Decisions in which the standard of reasonable care has been applied to determine whether the Federal Government has violated a fiduciary obligation to the Indians include: *Moose v. United States*, 674 F.2d 1277, 1283-84 (9th Cir. 1982); *Navajo Tribe of Indians v. United States*, 624 F.2d 981, 989 (Ct. Cl. 1980); *Coast Indian Community v. United States*, 550 F.2d 639, 652 (Ct. Cl. 1977); *cf., American Indians Residing on the Maricopa-Ak Chin Reservation v. United States*, 667 F.2d 980, 990, 993 (Ct. Cl. 1981), *cert. denied*, 456 U.S. 989 (1982).

ment may be liable for breach of standards applicable to a private trustee. *Mitchell II*, 463 U.S. at 226.

In both cases, this Court also laid out rules with respect to the use of common-law standards of conduct to determine whether the United States has acted in accordance with its fiduciary responsibilities. *Mitchell II* requires that when the Government serves as a trustee, its trust responsibilities, that is, its powers and its duties, are defined by the terms of the statute and the regulations which establish its fiduciary relationship with the Indians. *Id.* at 224. And *Mason* teaches that when a federal statute establishing an Indian trust does not define the standard which the Government must live up to, "familiar principles" from the law of trusts normally will do so. *Mason*, 412 U.S. at 398.

When the Court of Appeals' decision is read in light of these rules, its violation of them is obvious. First, in describing the Federal Government's trust responsibilities under the IMLA, the court failed to define the standard of conduct required of the Secretary—that is, the "contours" of his fiduciary responsibilities—by reference to the statute and the regulations which in unambiguous language confer upon the Secretary *the power to exercise discretion* in determining the Tribe's royalties. 25 U.S.C. § 396d (1982); 30 C.F.R. §§ 221.3, 221.4, 221.12, 221.40, 221.47 (1981); *see Mitchell II*, 463 U.S. at 224. The regulations and the IMLA Leases further define the exercise of the Secretary's discretion to include the acceptance of sales price as conclusive evidence of the royalty value of the gas. 25 C.F.R. § 221.13(a) (1982). Accordingly, by exercising his discretion in this manner, the Secretary also could not have abused or exceeded it, and thus he could not have violated a fiduciary duty to the Tribe in determining its royalties.[24]

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[24] Indeed, a Court of Appeals has described the regulatory provisions authorizing the Secretary to determine the value of the gas for royalty purposes as "extraordinary" and refused to allow the Secretary to apply the regulations retroactively to redetermine royalty liability. *Continental Oil Co. v. United States*, 184 F.2d 802,

Moreover, the terms of the IMLA and the regulations do not impose any duty on the Secretary which would prohibit the exercise of this discretion. Rather, the duty of the Secretary, as defined in the regulations, is to determine royalties based solely on the "reasonable value" of the gas. 30 C.F.R. § 221.47 (1981).

Because the regulations expressly define the contours of the Secretary's trust responsibility, there is no occasion to resort to common-law trust principles to further determine the scope of that responsibility. Had the Court of Appeals elected to examine the law of trusts, however, by placing reliance on this Court's decision in *Mason*, such an inquiry would have avoided the adoption of an erroneous standard of conduct. As Professor Scott has written:

> To the extent to which the trustee has discretion, the court will not control his exercise of it as long as he does not exceed the limits of the discretion conferred upon him. The Court will not substitute its own judgment for his.

III A. Scott, *supra*, p. 18, § 187 at 1501 (emphasis added).

Application of common-law trust principles also establishes that even when a trustee is under a duty to produce the "greatest return" or to act "in the best interests" of the beneficiary, the trustee commits a breach of duty in the exercise of discretion only if he acts beyond the bounds of reasonable judgment. *Id.* § 187.2 at 1514. Here, the Court of Appeals twice recognized that the decision of the Secretary to require dual accounting only by lessees who derived revenue from the sale of liquid by-products was reasonable, Jt. App. 45a, 48a; yet the court went on to overrule the Secretary's decision and to substitute its own judgment as to what was in the best interests of the Tribe.

The decision below is also in conflict with decisions of the Court of Claims. In *Mitchell v. United States*, 664

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821 (9th Cir. 1950); *cf. Atlantic Richfield Co. v. Hickel*, 432 F.2d 587 (10th Cir. 1970).

F.2d 265 (Ct. Cl. 1981), the court considered the appropriate standard for the imposition of liability against the United States for breach of trust. The regulations at issue in *Mitchell* had historically required the Government "to obtain the greatest revenue for the Indians . . . ." *See Mitchell II*, 463 U.S. at 224. Nevertheless, the Court of Claims held:

> [T]he standard by which Interior's actions are to be judicially tested is not the court's or plaintiff's own view of the preferable conduct, but the normal standard for government fiduciaries—were their actions in good faith and within the realm of their acceptable discretion, or were they arbitrary, capricious, an abuse of discretion, or contrary to law?

Mitchell, 664 F.2d at 274. In *Mitchell II*, this Court affirmed that decision, although it did not discuss the requisite standard of conduct. Since *Mitchell II*, the Court of Claims has continued to apply this standard. *Navajo Tribe of Indians v. United States*, 9 Cl.Ct 336, 344 (1986). The Court of Appeals' decision here is thus at odds not only with the precepts of *Mason* and *Mitchell II* but with the whole history of the law of federal fiduciary responsibility as developed in the *Mitchell* line of cases.

B. This Court Should Determine the Standard for the Government's Breach of Indian Trust Obligations Because of Its Fundamental Importance to the Discharge of Federal Fiduciary Duties.

In 1982 Congress enacted the Indian Mineral Development Act of 1982, 25 U.S.C. §§ 2101-2108 (1982). The House Report adopted prior to passage of the Act documents that Congress clearly understands the standard of conduct it has imposed on the Secretary in the performance of his fiduciary obligations respecting Indian oil and gas leases. The House Report reads:

> If the Secretary, acting as a trustee, approves a lease or an agreement or otherwise acts in relation to the trust resources of an Indian tribe and acts responsibily and within his discretion in doing so, the

> United States would not be liable for any loss or impairment of the trust resources. On the other hand, if the Secretary acts recklessly and in abuse of his discretion as trustee, the United States cannot avoid liability.

H.R. Rep. No. 746 on Indian Mineral Development Act of 1982, 97th Cong., 2d Sess., 7-8, *reprinted in* 1982 U.S. Code Cong. & Ad. News 3465, 3469-70.

Despite such explicit congressional guidance, the Secretary's management of Indian royalty matters continues to be subject to criticism,[25] and, as this case demonstrates, his determination of Indian royalties has been inconsistent.

Complaints of Government neglect of Indian trust responsibilities led the House Appropriations Committee this year to order its staff to investigate the Secretary's management. With respect to Indian oil and gas leasing, the staff report concluded that the Secretary still does not understand his fiduciary obligations to the Indians:

> [T]he Investigative Staff was unable to obtain consistent definitions of "Trust Responsibility" and "Self-Determination" or how the requirements of each could be combined to carry out BIA's leasing responsibilities of natural resources. *It should be noted that the Director, Office of Trust Responsibilities stated "* * * the term (Trust Responsibility) has no meaning" and also added "* * * whatever that means."*

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[25] *See* Indian Gov't Operations Comm., *Indian Gas Royalty Payments-Problems Persist* (July 19, 1985) cited in *Hearings on Department of Interior and Related Agencies Appropriations for 1987 Before the Subcomm. of the H.R. Comm. on Appropriations*, 99th Cong., 2d Sess., at 505 (Comm. Print 1986) (*"Hearings on Appropriations"*); *see also Interim BIA Task Force/Study Group Report on Indian Oil and Gas Lease Administration and Royalty Management* (Jan. 1985), quoted in *Hearings on Appropriations*, at 520.

Report of the Surveys and Investigations Staff, H.R. Comm. on Appropriations, at 2-3 (April 17, 1986) (emphasis added), quoted in *Hearings on Appropriations*, *supra* p. 26 n.25 at 517-18.

The Secretary's uncertain royalty administration is further confounded by the magnitude of reservation oil and gas production and resulting royalty revenues. Indian oil and gas reserves are located on forty reservations in seventeen states.[26] Under federal law the Secretary must determine tribal royalties from more than 4,000 Indian leases having more than 15,000 producing oil wells alone.[27] Since 1979, tribal oil and gas revenues have exceeded $200 million annually, and, if the Secretary has failed to fulfill his fiduciary duties during this period, it is estimated that lost Indian royalty revenues have been between $10 and $20 million annually.[28]

Whatever standard of conduct the Secretary is required to live up to, it is of vital importance that he know it and abide by it. Only then will lessees be able to transact business with Indian tribes on the basis of certainty and fairness. This petition presents this Court with an opportunity to speak authoritatively on the "contours" of the Federal Government's Indian trust responsibilities in the context of an activity that is a primary source of the Indians' livelihood, the continued development of their natural resources by non-Indians.

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[26] American Indian Policy Review Comm'n, *Final Report* 339 (1977).

[27] *Hearings on Appropriations*, *supra* p. 26 n.25 at 509.

[28] *Id.* at 507.

CONCLUSION

For the foregoing reasons, this Petition for a Writ of Certiorari should be granted.

Respectfully submitted,

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No. A-1010

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1986

SOUTHERN UNION COMPANY,
UNICON PRODUCING COMPANY,
SOUTHLAND ROYALTY COMPANY and
EXXON CORPORATION,
Petitioners,

v.

JICARILLA APACHE TRIBE,
DONALD P. HODEL, Secretary of the
United States Department of the Interior
and STATE OF NEW MEXICO,
Respondents.

PETITIONERS' JOINT APPENDIX TO PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

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APPENDIX A

UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

Nos. 81-1680
81-1860
81-1871
81-1872
81-1873
81-1874
81-1939

JICARILLA APACHE TRIBE,
Plaintiff, Appellant,
Cross-Appellee,

v.

SUPRON ENERGY CORPORATION,
SOUTHLAND ROYALTY COMPANY,
DONALD P. HODEL, Secretary of the Interior,
GAS COMPANY OF NEW MEXICO,
Defendants, Appellees,
Cross-Appellants,

EXXON CORPORATION,
Defendant, Cross-Claimant,
Appellee, Cross-Appellant,

STATE OF NEW MEXICO,
Applicant in Intervention
and Appellant in 81-1680.

[Filed Jan. 23, 1986]

U.S. District Court for the District of New Mexico
D.C. Civil No. 75-247M

ON REHEARING EN BANC

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Maria A. Iizuka, Attorney (F. Henry Habicht II, Assistant Attorney General, and Anne S. Almy, Attorney, Department of Justice, Washington, D.C.; William L. Lutz, United States Attorney, and Raymond Hamilton, Assistant United States Attorney, Albuquerque, New Mexico, with her on the brief), for Appellee, Cross-Appellant Donald P. Hodel, Secretary of the Interior.

John R. Cooney (Peter J. Adang and Susan R. Stockstill with him on the brief), or Modrall, Sperling, Roehl, Harris & Sisk, P.A., Albuquerque, New Mexico, for Appellee, Cross-Appellant Southland Royalty Company.

Mark F. Sheridan (Seth D. Montgomery, Gary R. Kilpatric, and Wesley B. Howard, Jr., with him on the brief), of Montgomery & Andrews, P.A., Santa Fe, New Mexico, for Cross-Appellant Gas Company of New Mexico.

Bruce D. Black of Campbell & Black, P.A., Santa Fe, New Mexico, filed a brief for Unicon Producing Company, formerly Supron Energy Corporation, Defendant, Appellee, Cross-Appellant.

Harold L. Hensley, Jr. of Hinkle, Cox, Eaton, Coffield & Hensley, Roswell, New Mexico, filed a brief for Defendant, Cross-Appellant Exxon Corporation.

Paul Bardacke, Attorney General, and Bruce Thompson, Assistant Attorney General, Santa Fe, New Mexico, filed a brief for State of New Mexico, Applicant in Intervention and Appellant in 81-1680.

Kenneth J. Guido, Jr., of Sonosky, Chambers, Sachse & Guido, Washington, D.C.; and Thomas Acevedo of Fredericks & Pelcyger, Boulder, Colorado, filed a brief for Amici Curiae Shoshone and Arapahoe Indian Tribes.

Ernest J. Altgelt III, Houston, Texas (John K. Dubiel and Thomas H. Burton, Houston, Texas; Jason Kellahin of Kellahin & Kellahin, Santa Fe, New Mexico; and Houston G. Williams of Williams, Porter, Day & Neville, Casper, Wyoming, appearing of counsel on the brief), for Amicus Curiae Conoco Inc.

Before HOLLOWAY, Chief Judge, SETH, MCWILLIAMS, BARRETT, DOYLE,* MCKAY, LOGAN, and SEYMOUR, Circuit Judges.

PER CURIAM:

These cases are before the court for rehearing en banc. The majority of the court adopts the prior dissenting opinion of Judge Seymour, reported at 728 F.2d 1555, 1563 (10th Cir. 1984), with the exceptions and additions set out below.

As Judge Seymour noted in dissent, whether the New Mexico Natural Gas Pricing Act (NMNGPA), N.M. Stat. Ann. § 62-7-1 et seq. (1982), applies to sales by non-Indian producers to non-Indian buyers of gas produced on the reservation is an issue that need not be decided in this case and we specifically do not decide it. We adopt the view that under the NMNGPA, value for royalty purposes can exceed sales prices and thus can exceed the price ceilings. Given this construction, the Act creates no possible conflict with federal law, so we need not decide the preemption issue addressed in the dissent.

There is one issue not reached in the dissent which must now be decided. The trial judge held that the Tribe had stipulated away part of its claim against de-

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* The Honorable William E. Doyle did not participate in this matter after December 31, 1985.

fendant Southland Royalty Company. The court said that "[a]cknowledging the inconsistency of this result, I state only that plaintiff is bound by the stipulation of counsel." 479 F. Supp. 536, 552 (D.N.M. 1979). The Tribe argues that the court's construction of its stipulation is not logical. Given the context in which the stipulation was made, we agree.

Prior to trial, the court granted partial summary judgment in favor of defendants on the issue of "value" for royalty purposes, holding that defendants had paid royalties on the "value" of minerals produced from the leased lands by basing royalties on the actual price received for sale of gas at the wellhead. Although the court ultimately reversed itself on this issue, its decision was the law of the case throughout the trial. The Tribe argues persuasively that when it stipulated, in the middle of the trial, that Southland had paid royalties at the appropriate rate on the consideration Southland had received, the stipulation only applied to the situation where the sale price had been held by the court to be conclusive evidence of value. On appeal, Southland has provided no reason why the Tribe would drop its claim against Southland and not against other defendants. We thus conclude that the trial court misconstrued the stipulation.

We have considered the other arguments of the various defendants and conclude that they are without merit. Accordingly, the district court is affirmed in all respects except for its limitation on the Tribe's recovery against Southland. In this regard, the cause is reversed and remanded to the district court for computation of the additional amount owing from Southland to the Tribe.

SETH, Circuit Judge, dissenting:

I must dissent from the majority opinion.

The panel opinion in this appeal noted that there was no finding that the Secretary had acted in an arbitrary or capricious manner in reaching and continuing his construction of the regulations and the lease as to royalty payments. This is mentioned because this finding has unusual implications in this case. Thus it has to be assumed that the Secretary had performed all his functions as a public official, and had considered his duties to carry out national energy policies; to exercise his discretion as to the subject matter under the regulations; to consider the impact on public land leases generally; to carry out contractual obligations; and his duties to the parties with direct concern—the Indian lessors and the lessees. These considerations were of both the short and long range implications of his action. Again, since the Secretary did not act in an arbitrary or capricious way, he included an evaluation of his position as to the lessors. There is nothing whatever shown to the contrary. The duty to the Tribe, however it may be characterized, was thus among the elements considered. His general broad discretion under the statutes, regulations, and the leases was, of course, an element in his evaluation.

The Secretary in the execution of his duties gave what he considered appropriate weight to each element. The majority of the panel which first heard the case concluded that he had acted within his duties and functions and thus held it was not for the trial judge to redo the Secretary's actions and assume his functions.

The trial court had substituted its own views as to the weight and consideration to be given to the several elements. The trial court thus overturned completely the construction of the regulations and the leases established by the Secretary for 20 or 25 years. This it did by considering only one element in the mix and excluding all

others. Thus the court held that the only factor or consideration was to "maximize" the immediate royalty revenues to the Jicarilla Apache Tribe. There was in its view nothing else to be considered. Thus, although the Secretary had evaluated all the elements and given weight to them (including a duty to the Tribe), he had in the court's view breached his fiduciary duty. This, again, because the Secretary's only duty was to "maximize" revenues and to do nothing else. If he did anything else it constituted a breach of "fiduciary duty." Under this view, of course, the Secretary had no discretion whatever under the regulations or leases, and no duty to the national energy policy, nor to public land policies, conservation or anything else. The only duty and function of the Secretary of the Interior was to "maximize" tribal revenues regardless. If this is his function he is not the Secretary of the Interior but a functionary for but one interest.

On the en banc consideration the Tribe again advances this only duty of the Secretary, but it fails to identify the extent, nature or the source of such a duty. It would not seem enough to pick up quotations from a variety of cases, and to apply them in this case regardless of context. There is no overall, all pervading "fiduciary duty" to the Tribe. It has to have its origin in some statute relating to the subject matter and applicable to the particular situation. This is what United States v. Mitchell, 445 U.S. 535, and United States v. Mitchell, 463 U.S. 206, teach. That is, there must be a statutory basis for the duty and a clear one. The particular statutes were brought forth in *Mitchell II*.

Congress has plenary power over the Indian tribes and their lands. A consideration of the relationships must start with this basic proposition. Congress has this complete authority and when it places with a public official the authority to perform a function and the power to control and to administer Indian property the grant must be clear and specific as to the particular property

before a fiduciary duty arises. This is what *Mitchell I* and *II* hold. There is only a "fiduciary duty" when a statutory basis exists and the nature and scope of such duty is therefrom clear. As the Court said, the statute defines the "contours" of a duty. Again, there is no amorphous all-inclusive "fiduciary duty" out there.

The Tribe itself entered into the leases as lessor. It has the authority that any lessor has under an oil and gas lease to enforce its terms and conditions and to so manage the property. The Tribe has engaged attorneys to provide advice. Its revenues from oil and gas royalties have been large as this record demonstrates. In *Mitchell I* the Court stated that Congress intended that the Indians were to manage their lands rather than the United States. This must be the starting point and the initial assumption in this case.

In *Mitchell II*, as mentioned, the Court relied on several *specific* statutory provisions relating only to Indians and to the subject concerned to have created a fiduciary duty. It held that to create a duty the statutes must "clearly establish" the fiduciary relationship. It is worthwhile to consider the statutes in *Mitchell II*: 25 U.S.C. §§ 406 and 407 refer to timber on Indian land held under a trust or other patent. It provides that timber sales shall be made upon a consideration of the "needs" and "best interests" of the Indian owner; 25 U.S.C. § 407 refers to sales of timber on unallotted reservation lands and provides such timber may be sold in accordance with sustained yield and with other standards *recited in the statute*; 25 U.S.C. § 466 directs the Secretary to make rules for the management of Indian forestry units; 25 U.S.C. § 318a covers roads on Indian reservations; § 323 empowers the Secretary to grant rights of way over Indian lands; § 324 covers consents for rights of way; and § 325 covers compensation. These were the specific statutes directed to Indian lands relied on by the Court in *Mitchell II*. The detail therein pro-

vided as to forestry practices demonstrate the needed detail to provide the existence and scope of the duty.

We have nothing comparable in the case before us. The plaintiffs seek to rely on the Indian Mineral Leasing Act, 25 U.S.C. § 396, to meet the "clearly establish" requirement, but its substance does not support such an argument. This Act does no more than authorize the Tribe to lease lands (with the approval of the Secretary) for minerals. Section 396(b) provides for bids for leases, but expressly provides that an organized Tribe (as here concerned) may lease according to its own constitution. Section 396(c) provides for bonds by lessees for compliance with leases and § 396(d) states that operations under the Indian leases shall be in accordance with rules and regulations promulgated by the Secretary. These are the general public land regulations and are not directed to Indian lands.

The General Allotment Act and the Indian Reorganization Act do not provide a basis for a fiduciary duty. Thus there are no prescribed standards—no "contours" for any management by the Secretary—only in accordance with the regulations *he prescribes.* This would seem at most to place his duty within a "reasonable care" standard along with everybody else.

There was no treaty with the Jicarilla Apaches. The Reorganization Act of 1934 does not supply a duty. There was no Congressional Act to create the Reservation.

Our cases, before *Mitchell I* and *Mitchell II,* rely on a general, all prevading "fiduciary duty," applicable in all dealings with Indian Tribes in all circumstances. Now however a fiduciary duty not only has to have its origin in statutory provisions, but it only has a meaning and scope derived therefrom. There is a new measure, a new standard, and the abundance of quotations

of phrases from the older cases would seem to be no longer useful.

The opinion of the Court in Nevada v. United States, 463 U.S. 110, is also significant as to several aspects of this case. It demonstrates the error in the remedy sought to be used by the trial court. Also, it considers circumstances where the Secretary of the Interior had duties in the same transaction to different entities one of which was the Pyramid Lake Paiute Tribe. The Court pointed out the diverse interests or claimants to the water there concerned and concluded that the Secretary had properly exercised his discretion. He had considered all elements and so discharged his duty. There is no hint in the opinion that the interest of the Paiute Tribe was the only consideration, and when it was included in the combined circumstances there was no breach of fiduciary duty as held by the trial court in the case before us. The fact that litigation was involved in *Nevada* v. *United States* is not significant as the action of the Secretary and his decision obviously preceded the litigation. The Court in *Nevada* v. *United States* said of the Secretary's several possibly conflicting obligations:

> "In this regard, the Government cannot follow the fastidious standards of a private fiduciary, who would breach his duties to his single beneficiary solely by representing potentially conflicting interests without the beneficiary's consent. The Government does not 'compromise' its obligation to one interest that Congress obliges it to represent by the mere fact that it simultaneously performs another task for another interest that Congress has obligated it by statute to do."

The Court in the same case quoted in a footnote the trial court's findings as to the conflict and which characterized the decisions in the Department as within the scope of delegated duties and which were political and policy decisions. Of this the Court said:

> "The District Court's finding reflects the nature of a democratic government that is charged with more than one responsibility; it does not describe conduct that would deprive the United States of the authority to conduct litigation on behalf of diverse interests."

It seems advisable to state a few facts in the case before us. The lease is the common form (or was) used for all public lands. The leases were executed by the Tribe and the original lessees in 1950. The gas produced is sold *at the wellhead* with a price adjustment for BTU content (thus the combustible gas and liquid content). The gas goes into *intrastate* commerce only. The Lybrook Plant near the Reservation extracts liquids from the gas produced by the leases in question and from gas produced elsewhere in the area from private and public lands. The liquid content of the gas varies from place to place. This plant operates most but not all the time. It is owned and operated by a stranger to the litigation. The extraction of liquids is for the transporters-owners of the gas which they have purchased at the wellhead from the defendant lessees. For a period of time, 1974-1979, the plant was owned by a defendant—Supron—but only for that period. No other lessee has had an interest in the plant. Extraction plants are common in and near gas fields throughout the country, including gas fields producing gas from the public lands under leases like the one in issue. The lessees were regularly billed for royalties by the USGS and its successor. These royalties were paid by the lessee-defendants. These computations were made in accordance with the Secretary's construction of the lease terms and regulations. The defendants thus acted only in response to the official line.

The regulations in issue need not be here described in detail. It is sufficient to point out that they divide, for the computation of royalty, lessees into two categories.

The first are the lessees with interests in an extraction plant, and for these the regulation 30 C.F.R. § 206.106 is directed to such a lessee which thereby derives revenues from the products extracted at its plant. Royalty is thus based on what such lessee receives for the products. The second group are the lessees who do not have an interest in such a plant and for these the Secretary has discretion to use the actual amount received at the wellhead for the gas produced or to use the highest field price (30 C.F.R. § 206.103) with the BTU adjustment.

The record shows that the Secretary put Supron in the first category during the period when it owned-operated the plant. This was the Secretary's construction of the regulations and the accepted practice. The other lessees were placed in the second category as were all lessees with no plant ownership. This was also the generally accepted construction of the leases and regulations and the one uniformly followed by the USGS for all public land leases.

The trial court instead sought to place the lessees in both categories at the same time in requiring that royalties be computed on the higher of the two figures. There is no basis in the regulations to place a lessee in both. It thus required accounting from lessees as to product values and processing costs although strangers owned the plants and lessees had no access to the plant records. There was however a theoretical formula provided in the regulations.

The method the trial court devised was also incomplete in several important particulars. It made no allowance for shrinkage or line losses, for drip gasoline, or for the cost of transportation to the plant. The theoretical manufacturing allowance departed widely from the standards theretofore applied, and had no basis in the record. There are other omissions which demonstrate it was a matter to be left to the experts. The solution by the trial court also ignored the fact that the propane and butane

are further processed. It is just as reasonable to include this processing as it is the processing of the gas. The trial court's solution treats these leases differently from public land leases nearby under the very same regulations.

It became more apparent during the en banc oral argument that if it were held that there was a breach of duty by the Secretary the trial court applied the remedy to the wrong parties and so punished the lessees although it stated that they were in no way at fault. They paid what they were billed. It was also observed at the oral argument that the Tribe had an action pending against the Government in the Claims Court asserting a breach of duty arising from the same circumstances.

It has been suggested that some sort of a break in the sequence should be made in 1979 when the Secretary acceded to the trial court's orders. That somehow the dual accounting arose as an independent act of the Secretary. The record does not permit this independent act argument as the change came about only as a response to the order of the trial court. There is no administrative record to support such a 'voluntary" change as is required.

The timing and the statements or references to the orders also demonstrate the involuntary nature of the change. However, equally persuasive was the argument of the Government at the en banc hearing which recited that before the court order there were some persons in the department seeking a change and some memos written, but they were unable to get official approval for a change.

It is also persuasive that these are the *only* Indian or public land leases in the country where this construction is now applied. If this is the only place it cannot be accepted that the change was voluntary. If the Secretary independently came to a decision to require dual account-

ing and to so change the long construction of the lease and regulations it was necessary for him to articulate the reasons for the change. Motor Vehicle Manufacturers Ass'n v. State Farm Mutual Automobile Insurance Co., 463 U.S. 29. This is both a procedural and substantive requirement. This was not done. It would have been necessary and the practice to give notice to those directly concerned to give them a chance to express their views. Again, there is no administrative record to describe or to support such a change. The conclusion must be reached that the change was not an administrative change but was instead brought about by the trial court's order.

The order was entered April 11, 1979. The Secretary relies on memos which did not reach the problem. This is particularly evident in an Associate Solicitor's letter of July 20, 1981. There is reliance for independent action placed on the IBLA *Supron* opinion, but this relies on the trial judge's order. This opinion expressly refers to "[w]here a United States District Court has ordered a lessee to adopt dual accounting . . . ." In any event, the issue in the above *Supron* case only arose as to Supron's interest in the Lybrook plant described above and was in conformity with the then existing construction. It did not concern other lessees.

In the record no basis exists for a conclusion that the change in the Secretary's position as to dual accounting came about other than by the court's order. Again, it should be mentioned that the Government's oral argument at the en banc hearing stated that there were internal memos in the Department on the subject of dual accounting, but it had no official sanction before the court order. Again, these are the *only* Indian or public land leases in the country where dual accounting is required. This has continued since the purported change five or eight years ago. This must have some significance.

Thus the infirmities both substantive and procedural of the trial court's order continues to this day. If the

dual accounting is supported it must be by reliance on the actions of the trial court.

I would set aside the order and judgment of the trial court.

Judge McWilliams and Judge Barrett join in this dissenting opinion.

MARCH TERM—April 15, 1986

Before Honorable William J. Holloway, Jr., Honorable Oliver Seth, Honorable Robert H. McWilliams, Honorable James E. Barrett, Honorable Monroe G. McKay, Honorable James K. Logan, Honorable Stephanie K. Seymour, Honorable John P. Moore, Honorable Stephen H. Anderson, Honorable Deanell Reece Tacha, Honorable Bobby R. Baldock, Circuit Judges

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Nos. 81-1680
81-1860
81-1871 thru 81-1874
81-1939

JICARILLA APACHE TRIBE,
Plaintiff-Appellant/
Cross-Appellee,

vs.

SUPRON ENERGY CORPORATION, *et al.*,
Defendants-Appellees/
Cross-Appellants.

This matter comes on for consideration of the petitions for rehearing and suggestions for rehearing en banc filed in the captioned cause by Defendants-Appellees/Cross-Appellants Unicon Producing Company (formerly Supron Energy Corporation), Gas Company of New Mexico, and Exxon Corporation.

Upon consideration whereof, the petitions for rehearing are denied by the en banc court that rendered the decision sought to be reheard. Judge Barrett voted to grant rehearing.

A poll was requested on the en banc suggestion. Judges Barrett and Baldock voted to grant rehearing en banc. A majority of judges having voted to deny the petition for rehearing en banc, the petition is therefore denied.

/s/ Robert H. Hoecker
ROBERT H. HOECKER
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MAY TERM—June 18, 1986

Before Honorable William J. Holloway, Jr., Honorable Oliver Seth, Honorable Robert H. McWilliams, Honorable James E. Barrett, Honorable Monroe G. McKay, Honorable James K. Logan, Honorable Stephanie K. Seymour

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Nos. 81-1680
81-1860
81-1871 thru 81-1874
81-1939

JICARILLA APACHE TRIBE,
Plaintiff-Appellant/
Cross-Appellee,

vs.

SUPRON ENERGY CORPORATION, *et al.*,
Defendants-Appellees/
Cross-Appellants.

The Government has moved the Court to modify its en banc opinion in this case with respect to various conclusions regarding the Secretary's fiduciary duty to the Tribe. Upon consideration, the motion to modify in the regard requested by the Government is denied. Judges Seth and Barrett would grant the Government's motion.

On its own motion, the Court hereby supplements the en banc opinion. Citing *Nevada v. United States*, 463 U.S. 110, 114 n.16 (1983), defendants have argued that the Government should pay the additional royalties owing as the result of this case because their nonpayment resulted from the Government's breach of its fiduciary duty.

We disagree. The allegation in *Nevada* was that the Government ineffectively represented the Tribe in a lawsuit, resulting in the Tribe being barred by res judicata from raising claims against third parties. The Court said in note 16 that the Tribe's remedy was against the Government. While the Secretary failed in its duty to represent the Tribe's interests in the present case, the relationship between the Tribe and defendant-lessees is contractual. The failure of the Secretary to require dual accounting resulted in the lessees paying an insufficient amount of royalties under the contract. That the Secretary breached its fiduciary duty to properly enforce the leases does not excuse the lessees from subsequently having to pay the amounts determined to be owed under the leases. *Cf. Atlantic Richfield Co. v. Hickel*, 432 F.2d 587, 592 (10th Cir. 1970).[1]

The mandate in this case is stayed for 30 days to permit the timely filing of a petition for writ of certiorari. If a timely petition is filed, the stay shall remain in effect until the Supreme Court disposes of the petition.

/s/ Robert L. Hoecker
ROBERT L. HOECKER
Clerk

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[1] Judges Seth, McWilliams, and Barrett dissent from this conclusion.

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APPENDIX B

UNITED STATES COURT OF APPEALS
TENTH CIRCUIT

Nos. 81-1680
81-1860
81-1871
81-1872
81-1873
81-1874
81-1939

JICARILLA APACHE TRIBE,
Plaintiff, Appellant,
Cross-Appellee,

v.

SUPRON ENERGY CORPORATION,
SOUTHLAND ROYALTY COMPANY,
JAMES G. WATT, Secretary of the Interior,
GAS COMPANY OF NEW MEXICO,
Defendants, Appellees,
Cross-Appellants,

EXXON CORPORATION,
Defendant, Cross-Claimant,
Appellee, Cross-Appellant,

STATE OF NEW MEXICO,
Applicant in Intervention and
Appellant in 81-1680.

[Filed Feb. 24, 1984]

Appeal from the United States District Court
For The District of New Mexico
(D.C. Civil No. 75-247 M)

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Thomas L. Dunigan, Assistant Attorney General, State of New Mexico (Jeff Bingaman, Attorney General, and Bill Primm, Assistant Attorney General, with him on the brief), Santa Fe, New Mexico, for State of New Mexico, Applicant in Intervention and Appellant in 81-1680.

Kenneth J. Guido, Jr., Reid Peyton Chambers, Harry R. Sachse, Lloyd B. Miller, Kevin A. Griffin and Loftus E. Becker, Jr. of Sonosky, Chambers, Sachse & Guido, Washington, D.C., filed a brief on behalf of Amici Curiae Shoshone and Arapahoe Indian Tribes.

Before SETH, Chief Judge, McWILLIAMS and SEYMOUR, Circuit Judges.

SETH, Chief Judge.

These are consolidated actions and appeals wherein the plaintiff asserts a series of claims arising from oil and gas leases executed 25 or 30 years ago. There are several separate issues raised on appeal concerning computation of royalty, development and antitrust claims. The gas production was from wells located on the Jicarilla Reservation and was sold and consumed in New Mexico.

Issues Relating to Value of Gas

The trial court held for all practical purposes that the defendants should have paid royalty computed on a "value" which was derived from the total net amount realized by the Lybrook processing plant for all products it developed from the gas it received from Southern

Union which in turn had been purchased from and at the leases of the defendants on the Jicarilla Indian lands.

The court required that there be a "dual accounting" by all lessees which meant that there be determined both the price received by the lessees for wet gas at the wellhead where title passed, but adjusted for btu content; and secondly, that there be ascertained the value of the several products derived from the gas stream, and sold by the Lybrook plant operator/owner. This product figure was to be a net figure or "net realization." The trial court held that the royalty from all leases concerned should be computed on the larger of the two figures. The court thus mandated that the "value" based on plant product values (or net realization) be determined, and be used as an alternate whether or not the lessee paying the royalty had any interest in the processing plant and whether or not the lessee received any added compensation for the products developed by the plant. This blanket requirement was contrary to the position taken by the Secretary through the years. The requirement of "dual accounting" required of all lessees by the trial court is one of the several basic issues raised on this appeal. It has a facet which involves the Secretary of Interior as the trial court also held that this dual accounting should have been required by the Secretary from the outset and since it was not done there was thereby a breach of fiduciary duty.

The leases were executed in the early 1950's and the regulations then in effect were not changed since that time in any respect material to this problem up to the time in 1979 when the trial court entered orders directed to dual accounting. From 1950 to 1979 without exception, and without variation, the Secretary and the USGS had construed the lease provisions and the regulations to require dual accounting not by all lessees, but *only* in instances where the lessee owned the processing plant (or received added money for its products).

The trial court's holding was thus contrary to a long uniform administrative construction and application of the regulations and the lease provisions. The trial court did not build on any basis in the administration actions, but instead developed a wholly new interpretation. It made no finding that the Secretary or the USGS had acted through the years with any abuse of discretion or in an arbitrary and capricious manner.

The record shows that Supron was the only defendant which at any material time had an interest in the Lybrook plant. This interest was recognized at the time it existed by the USGS in its construction of the lease and regulations. Thus royalty requirements and reports by it were based on product value. This is an example of the consistent application of administrative construction. Since no other defendants had such an interest no such requirement was placed on them until the trial court sought to apply product values to all lessees although the plant was operated/owned by strangers whose operations and costs were not before the court and no reason was advanced as to why they would be made available to the defendants. The plant also processed gas from the general area thus from leases not here concerned. It is located outside of and about 20 miles west of the reservation boundary.

Lease Provisions

The lease provision in paragraph 3(c) [in Southland leases] provides that the royalty at 16⅔% be computed on:

> "the value or amount of all oil, gas, and/or natural gasoline, and/or all other hydrocarbon substances produced and saved from the land leased herein . . . ."

The lease form [Southland] provides that the Secretary has discretion to ascertain "value" for the computation. Thus paragraph 3(c) provides also that:

> "During the period of supervision, 'value' for the purposes hereof may, in the discretion of the Sec-

> retary, be calculated on the basis of the highest price paid or offered (whether calculated on the basis of short or actual volume) at the time of production for the major portion of the oil or the same gravity, and gas, and/or natural gasoline, and/or all other hydrocarbon substances produced and sold from the field where the leased lands are situated, and the actual volume of the marketable product less the content of foreign substances as determined by the oil and gas supervisor. The actual amount realized by the lessee from the sale of said products may, in the discretion of the Secretary, be deemed mere evidence of or conclusive evidence of such value. When paid in value, such royalties shall be due and payable monthly on the last day of the calendar month following the calendar month in which produced; when royalty on oil produced is paid in kind, such royalty oil shall be delivered in tanks provided by the lessee on the premises where produced . . . ."

It appears that the royalty provisions are directed to production and sale at the field thus "produced and sold from the field." The due date for royalty payments is related to the month "in which produced" thus produced from the ground. When royalty oil is paid in kind it is to be delivered on the "premises."

The phrase "[t]he actual amount realized by the lessee from the sale of said products" referred back to oil, gas, natural gasoline, and "all other hydrocarbon substances produced and sold from the field." This portion is clearly limited by the first few words—"[t]he actual amount realized by the lessee." The "actual amount realized" can apply under the Secretary's construction to a lessee who realizes amounts from products sold or from *his* extraction plant but to those situations only.

The lease makes specific reference to the value of products of gas for royalty purposes to allow for the

cost of manufacture as one choice with the "value" of the gas as the other. Thus:

> "It is understood that in determining the value for royalty purposes of products, such as natural gasoline, that are derived from treatment of gas, a reasonable allowance for the cost of manufacture shall be made, such allowance to be two-thirds of the value of the marketable product unless otherwise determined by the Secretary of the Interior on application of the lessee or on his own initiative, and that royalty will be computed on the value of gas or casinghead gas, or on the products thereof (such as residue gas, natural gasoline, propane, butane, etc.), whichever is the greater."

This provision gives the typical gas value versus a rough net "value" of the product. This lease provision refers to the determination of the "value for royalty purposes of products." It thus describes what is to be done if royalty is to be applied to "products," but it does not say under what circumstances royalty shall be computed on products.

As described above, the Secretary has construed the lease and the regulations to require a computation based on products only when the lessee is the owner of the plant producing the products or on those who realize direct income from the sale of products.

Despite the several sentences following it, the controlling limitation as to royalty is the phrase "the actual amount realized," and the subsequent provisions are directed to such a determination with formulas and choices to accomplish that end.

Regulations

The regulations expand on the several lease provisions quoted above and quote portions, thus 30 C.F.R. § 171.13, 30 C.F.R. § 221.47, 30 C.F.R. §§ 221.51 and 221.52.

30 C.F.R. § 221.50 makes reference to products and subsection (b) provides:

> "If the lessee derives revenue on gas from two or more products, a royalty normally will be collected on all such products."

This is specific as to a lessee who "derives revenue" on gas from products will pay a royalty on all such products. Again, the term "derives revenue" points only to a lessee who has a processing plant or a contract to share in the sale of products.

Section 221.50(c) provides:

> "For the purpose of computing royalty, the value of wet gas shall be either the gross proceeds accruing to the lessee from the sale thereof or the aggregate value determined by the Secretary of all commodities, including residue gas, obtained therefrom, whichever is greater."

It appears that the trial court placed its principal reliance on this subparagraph (c) in arriving at an independent judgment as to the proper construction of the lease.

We cannot agree with the trial court that this subsection by itself or together with other regulations or lease terms is sufficient to set aside the Secretary's construction of his regulation and lease which was followed and applied without exception for these many years, a construction which has a perfectly reasonable basis in the lease and in the regulations. Furthermore it was and is in conformance with the practices in the industry as shown by the record.

We cannot overlook the express provision in the lease which states relative to "value" for royalty:

> "The actual amount realized by the lessee from the sale of said products may, in the discretion of the

> Secretary, be deemed mere evidence of or conclusive evidence of such value."

The regulations contain similar provisions. These clear grants of authority cannot be ignored in assessing the discretion of the Secretary.

We have described and quoted at some length the lease clauses and the pertinent provisions of the regulations. This has been done not to determine whether or not we agree with the administrative interpretation, but instead to describe the issue and to show the basis for the Secretary's position. When the prevailing doctrine in this circuit is then applied to these circumstances we must conclude that the administrative interpretation which prevailed through the years must be applied.

We have found no abuse of discretion in this respect by the Secretary and the trial court found none. There is no indication of action by the Secretary which could be characterized as arbitrary or capricious. The Secretary's position is consistent with case law in this circuit. *See* Barby v. Cabot Corporation, 465 F.2d 11 (10th Cir.).

The trial court's determination that dual accounting is required of all lessees must be and is set aside. The original construction placed on the lease and regulations by the Secretary as to this issue must be applied to and through the conclusion of these proceedings. The Secretary and the IBLA appear to have changed their positions in response to rulings on the point by the trial court during these proceedings.

Fiduciary Duty of the Secretary

As noted above, the trial court held that the Secretary of Interior violated fiduciary standards in not applying the royalty provisions in the way in which the court construed them. In view of our holding above as to the basis for the Secretary's construction, in view of the discretion vested in the Secretary as to the regulation of

oil and gas matters, in the absence of any finding or indication of abuse of discretion, and in view of the conformance of the construction to the general practices in the industry and the controlling case law, we find no basis for the trial court's determination as to fiduciary standards. We need not and do not decide whether or not the Secretary owes the tribe a fiduciary duty as to the matters under consideration.

Gas Volumes

We have concluded that the trial court was correct in its holding that the volume measurements of gas in the past were correct as was the application of field prices. These points are fully developed in the record and by the trial court and no purpose would be served by a review of the facts in this opinion.

Lease Development

The trial court held that there was no proof adduced to demonstrate a lack of development under the leases. This matter was so examined under the legal standards applicable to the circumstances which are well developed. This is a much litigated matter and there are well defined standards. The trial court applied these to the facts and we agree with the conclusion so reached.

Since there was no violation of lease terms or regulations as to development of the leaseholds, we do not reach the question as to whether the Secretary had a fiduciary duty as to this matter. The Secretary necessarily functioned within the lease terms and the regulations.

Antitrust Issues

In its complaints the plaintiff advanced several antitrust claims based on alleged price-fixing by the defendants. In this position plaintiff's reliance was placed on the most part on the fact that long-term gas purchase

contracts had been entered into between the lessees and Southern Union, the gas purchaser. The court found no evidence of price-fixing or restraint of trade. It found that the gas purchase contracts were typical since the 1930's of those used in the San Juan Basin by other purchasers. The court found that the contracts entered into by the lessees although similar in form were the result of independent business judgments and sound business reasons were evident.

The trial court laid particular emphasis on the uniform use by Southern Union of most favored nation clauses in its gas purchase contracts throughout the San Juan Basin. We agree that this is a significant factor. The price evidence before the court demonstrates that the prices were generally in accordance with the national trends. The tribe in 1976 sought to sell its royalty gas to Southern Union at the same price.

As to the liquids produced at the Lybrook plant the evidence showed that they were but a very small part of the market. Supron produced when it operated the plant no more than a 3% market share. Southern Union also had a relatively small share of the market for liquids in the Basin. Southern Union purchased about 4% of the gas produced in the market area.

The extent of the market as determined by the trial court—the San Juan Basin—is a factual matter. The definition of a relevant market is a factual matter, only to be disturbed if the trial court's finding was clearly erroneous. Telex Corp v. IBM, 510 F.2d 894 (10th Cir.). The basis of the determination is the interchangeability of the product controlled with other available products. United States v. Du Pont & Co., 351 U.S. 377. We must hold that the trial court's finding is correct and supported by the record.

There existed some interlocking directors and some corporate affiliations from time to time. There were a

series of reorganizations and mergers. The trial court concluded as to section 8 of the Clayton Act there may have been some technical violations. The tribe was, however, unable to show any ill effects flowing from interlocking directorships in some of the defendant companies. In the absence of proof of anticompetitive effects, the tribe could prevail only if interlocking directorships was a *per se* violation of the Sherman Act. The Supreme Court has shown great reluctance to add to the short list of types of economic activity that are *per se* Sherman Act violations. White Motor Co. v. United States, 372 U.S. 253. A *per se* violation is a naked restraint of trade with no purpose except to stifle competition. The tribe has not shown that interlocking directorships have this kind of "pernicious effect on competition and lack of any redeeming virtue." Northern Pac. R. Co. v. United States, 356 U.S. 1, at 5. We agree with the trial court that the tribe has not made out a case for damages under section 8 of the Clayton Act. Section 8 forbids interlocking directorships, and there may have been a technical violation of this provision. However, the tribe offers only speculation on possible ill effects of interlocking directorships and no evidence of injury caused by a possible violation. It may be true that such a situation may indicate an opportunity to conspire, but affiliation does not by itself necessarily imply conspiracy to restain trade. H & B Equipment Co., Inc. v. International Harvester Co., 577 F.2d 239 (5th Cir.); Knutson v. Daily Review, Inc., 548 F.2d 795 (9th Cir.). We affirm the trial court's holding that the tribe failed to carry its burden of showing injury that is connected in a causal manner to the violation. Gottesman v. General Motors Corporation, 436 F.2d 1205 (2d Cir.).

The State Law Ceiling on Gas

The trial court held that the New Mexico Natural Gas Pricing Act, § 62-7-1 N.M.S.A. 1978, did not apply to gas produced on the Jicarilla reservation. We must re-

verse this determination because there are no exceptions to the application of the state statute in its control of ceiling price on intrastate natural gas, and we conclude that the decisions of the Supreme Court demonstrate that the state statute does apply to the gas sales here under consideration.

The method for computing royalty is fixed in the lease which created the business relationship between the lessor and lessee, and which also granted the lessee an interest in the land. We have in this opinion described the pricing or value for royalty purposes. It is basically a field price in a large producing area and the ceiling price is fixed by federal and state laws as a price control designed to protect the ultimate gas consumers from excessively high prices. These ceilings necessarily override contractual relationships and there are no exceptions based on who the royalty owner may be. It appears that the State of New Mexico as a royalty owner is subject to the ceilings. It is a limit on the size of the royalty owner's check and the lessee's check .

The transaction here concerned is a sale to non-Indians on the reservation. This is the source of income to the tribe from the commercial and land ownership arrangement. The limit is thus on income as in Moe v. Salish & Kootenai Tribes, 425 U.S. 463, and in Washington v. Confederated Tribes of Colville Indian Reservation, 447 U.S. 134. We must hold that the determination of this issue is controlled by the two cited cases.

There is by reason of the state price control act an effect on the money the tribe receives from the sales but there is no direct conflict with Indian self-government.

The relationship is with non-Indians as mentioned—sales on the reservation to non-Indians. In this respect we must consider the recent opinion of the Supreme Court in Montana v. United States, —— U.S. ——, 49 U.S.L.W. 4296, and in United States v. Wheeler, 435 U.S. 313. In

Montana, the Court quoting from *Wheeler* said of the tribe's right over the entire reservation:

> " 'The areas in which such implicit divestiture of sovereignty has been held to have occurred are those involving the relations between an Indian tribe and nonmembers of the tribe . . . .
>
> " 'These limitations rest on the fact that the dependent status of Indian tribes within our territorial jurisdiction is necessarily inconsistent with their freedom independently to determine their external relations. But the powers of self-government, including the power to prescribe and enforce internal criminal laws, are of a different type. They involve only the relations among members of a tribe.' "

The Court in *Montana* also said that the "exercise of tribal power beyond what is necessary to protect tribal self-government or to control internal relations is inconsistent with the dependent status of the tribes, and so cannot survive without express Congressional delegation."

The Court in Merrion v. Jicarilla Apache Tribe, 455 U.S. 130, at 138, refers to the sharp distinction between Indian taxing acts and the lease covenants. It there said:

> "As we observed in *Colville*, *supra*, the tribe's interest in levying taxes on nonmembers to raise 'revenues for essential governmental programs . . . is strongest when the revenues are derived from value generated on the reservation by activities involving the Tribes and when the taxpayer is the recipient of tribal services.' 447 U.S., at 156-157. This surely is the case here. The mere fact that the government imposing the tax also enjoys rents and royalties as the lessor of the mineral lands does not undermine the government's authority to impose the tax. See *infra*, at 145-148. The royalty payments from the mineral leases are paid to the Tribe in its role as

> partner in petitioners' commercial venture. The severance tax, in contrast, is petitioners' contribution 'to the general cost of providing governmental services.' "

In conclusion on the issue of the effect of the state price limitation it should be mentioned that a state regulation of prices is expressly provided for in the federal statute. Section 602(a) of the National Gas Policy Act of 1978 (15 U.S.C. § 3001 *et seq.*). Also the Conference Report on the National Gas Act states in part that the reference to state authority to control expressly states that authority is thereby "ceded" under the Commerce Clause to regulate prices to "affected states." This in itself would seem to answer a claim that state price control does not apply to the intrastate gas. Thus such state price control prices are applicable and further the federal price control prices are applicable to royalties.

The judgment of the trial court is affirmed except as to:

1. The dual accounting/value of gas issue, and as to this it must be reversed and the matter is instead to be controlled by the long-standing and pre-litigation administrative construction of the leases and regulations. The judgment must also be reversed as to the related holding of breach of fiduciary duty by the Secretary.

2. We must also reverse as to the application of state price control as hereinabove described, and we also hold that federal price control prices are applicable in the determination and computation of royalty.

SEYMOUR, J., concurring in part and dissenting in part.

I concur in the majority's holding on the antitrust issues for the reasons set out in Part IV below. However, I cannot agree with the remainder of the majority's opinion. The court today declares that it can determine whether the Secretary properly interpreted and applied regulations dealing with royalties from resources owned by the Jicarilla Apache Tribe without first deciding whether the Secretary owes any duty of trust to the Tribe in these activities. The majority then rejects the trial court's interpretation of those regulations. Finally, the court holds that the New Mexico Natural Gas Pricing Act, N.M. Stat. Ann. §§ 62-7-1 to -10 (1978) (NMNGPA), can function to diminish tribal royalties. Because I cannot agree with any of these conclusions, I must respectfully dissent.

I.

TRUST RESPONSIBILITIES

If the Secretary is obligated to act as a fiduciary to the Tribe in his administration of the Tribe's oil and gas reserves, and in his determination of what royalties the Tribe is due, then his actions must not merely meet the minimal requirements of administrative law, but must also pass scrutiny under the more stringent standards demanded of a fiduciary. Therefore, the need to determine whether the Secretary owes any duty of trust to the Tribe is unavoidable.

The notion that the Secretary, as a representative of the federal government, stands in a special relationship in general to the Indian tribes is not a novel proposition and needs neither extensive discussion nor citation. *See, e.g., United States v. Kagama*, 118 U.S. 375, 383-84 (1886); *Cherokee Nation v. Georgia*, 30 U.S. (5 Pet.) 1, 17 (1831). The Supreme Court has continually recognized "the distinctive obligation of trust incumbent upon

the Government," *Seminole Nation v. United States*, 316 U.S. 286, 296 (1942), in its dealings with the Indian tribes.[1] *See, e.g., United States v. Mitchell (Mitchell II)*, 103 S.Ct. 2961, 2972 (1983). Because of this trust relationship the Government, in both its executive and legislative branches, is held to a high standard of conduct, one consonant with its "moral obligations of the highest obligation and trust." *Seminole Nation v. United States*, 316 U.S. at 297. For the same reason, whenever doubt or ambiguity exists in federal statutes or regulations, such doubt is resolved in favor of the tribes. *See, e.g., Bryan v. Itasca County*, 426 U.S. 373, 392 (1976).

In addition to the all-pervasive "general trust relationship between the United States and the Indian people . . . [that] has long dominated the Government's dealings with Indians," *Mitchell II*, 103 S.Ct. at 2972, the Supreme Court has declared that other, context-specific trust relationships of varying depth and responsibility exist. *Id.; compare United States v. Mitchell (Mitchell I)*, 445 U.S. 535, 542, 546 (1980) (General Allotment Act creates a limited trust relationship, not a fiduciary responsibility for management of allotted forest lands) *with Mitchell II*, 103 S.Ct. at 2972 (other federal statutes and regulations establish a full fiduciary relationship in management of allotted forest lands).

Both the Supreme Court and this circuit have recently set out the test for determining a trust relationship. In *Whiskers v. United States*, 600 F.2d 1332 (10th Cir. 1979), *cert. denied*, 444 U.S. 1078 (1980), we made it clear that no particular words or phrases are critical to

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[1] The Government's willing assumption of its obligations to Indian tribes is exemplified by the language of the treaty entered into July 1, 1852 in Santa Fe with the Apache Nation. Article 11 of the Treaty contains the promise "that the government of the United States shall so legislate and act as to secure the permanent prosperity and happiness" of the Apache Nation. Treaty with the Apaches, 10 Stat. 979, 980 (1855).

the finding of a trust relationship. "[T]he use of the word 'trustee' is not absolutely essential to the finding of a trust relationship when it is otherwise clear that Congress intended a trust relationship to exist." *Id.* at 1338. Rather, the test is whether "the relevant statutory and regulatory provisions [contain] an enumeration of duties which would justify a conclusion that Congress intended the Secretary to be a trustee." *Id.* In *Mitchell II*, the Court reviewed the statutes and regulations establishing the particular relationship between the government and the Indians to determine whether they "give the Federal Government full responsibility to manage Indian resources and land for the benefit of the Indians." 103 S.Ct. at 2972. Finding that they did so, the Court concluded, "[t]hey thereby establish a fiduciary relationship and define the contours of the United States' fiduciary responsibilities." *Id.*

In *Mitchell II*, the Supreme Court determined that the Secretary owed Indian tribes a duty of trust in administering the sale of timber on Indian lands. Because the statutory and regulatory scheme in *Mitchell II* parallels that involved here, I believe *Mitchell II* governs the resolution of this issue.

In finding a trust relationship in *Mitchell II*, the Court noted that the Secretary plays a "pervasive role" in sales of timber from Indian lands. 103 S.Ct. at 2969. The Court then carefully examined the statutes dealing with sales of timber on reservation land, the legislative history underlying the statutes, and the regulations explicating them, finding it significant that "[t]he Department of the Interior . . . 'exercises literally daily supervision over the harvesting and management of tribal timber.' . . . Virtually every stage of the process is under federal control." *Id.* at 2971 (quoting *White Mountain Apache Tribe v. Bracker*, 448 U.S. 136, 147 (1980)) (footnote omitted). The Court found that "the Government has 'expressed a firm desire that the Tribe should

retain the benefits derived from the harvesting and sale of reservation timber,'" *id.* at 2972 (quoting *White Mountain Apache Tribe v. Bracker*, 448 U.S. at 149). Accordingly, it held that a fiduciary relationship was established.

In addition to finding a trust duty expressed in the statutes and regulations, the Court declared that

> "a fiduciary relationship necessarily arises when the Government assumes such elaborate control over forests and property belonging to Indians. All of the necessary elements of a common-law trust are present: a trustee (the United States), a beneficiary (the Indian allottees), and a trust corpus (Indian timber, lands, and funds). '[*W*]*here the Federal Government takes on or has control or supervision over tribal monies or properties, the fiduciary relationship normally exists* with respect to such monies or properties (unless Congress has provided otherwise) *even though nothing is said expressly in the authorizing or underlying statute* (or other fundamental document) about a trust fund or a trust or fiduciary connection.' *Navajo Tribe of Indians v. United States*, 224 Ct. Cl. 171, 183, 624 F.2d 981, 987 (1980)."

Id. (footnote omitted) (emphasis added).

Leasing of minerals located on Indian reservations is also a creature of federal statute. As in timber harvesting, the federal government's role in mineral leasing is pervasive and its responsibilities comprehensive. The Indian Mineral Leasing Act of 1938, 25 U.S.C. §§ 396a-396g (1976), requires the Secretary to: set the "terms" and "conditions" for leasing, *id.* § 396b; approve leases, *id.* § 396a; establish lease sale procedures, *id.* § 396b; reject unsatisfactory bids, *id.*; require satisfactory performance bonds of lessees, *id.* § 396c; promulgate rules and regulations governing "all operations" under leases,

id. § 396d; and approve leases for subsurface storage when necessary to avoid waste, or to promote conservation of resources, or to protect tribal welfare, *id.* § 396g. The evident purpose of the statute is to ensure that Indian tribes receive the maximum benefit from mineral deposits on their lands through leasing.

This interpretation is supported by the Act's legislative history. When the Act was proposed, the Secretary of the Interior urged that the legislation be enacted because "it is not believed that the present law is adequate to give the Indians the greatest return from their property." Senate Report No. 985 at 2 (1937); House Report No. 1872 at 2 (1938). Congress responded to the need to ensure that the Indians' welfare be protected and their natural resources be managed to the tribes' maximum benefit by emphasizing the Secretary's fiduciary obligations, directing the Secretary to approve lease sales only when they are "in the interest of the Indians." *Id.*

Interior has promulgated extensive regulations for managing leases under the Act. *See* 25 C.F.R. pt. 211 (1982). The regulations stress that the Secretary must act in the best interests of the tribes. *See, e.g., id.* §§ 211.3(b), .6(a), .9(b)(1), .12(a), .19, .21(a), .22, .27. Additional regulations, published in 30 C.F.R. Part 221, require the government to maintain comprehensive records of price and production, and to determine royalties 30 C.F.R. § 221.12. These regulations detail in exhausting thoroughness the government's management and regulatory responsibilities. *See id.* pt. 221.

Because the statutes and regulations contain such an explicit and detailed enumeration of duties, in my view *Mitchell II* compels the conclusion that Congress intended the Secretary to be a trustee.[2] *See* 103 S.Ct. at 2971-72.

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[2] This conclusion is supported by the Supreme Court's resolution of a case involving Interior-approved oil and gas leases on lands

II.

BREACH OF TRUST

The trial court in this case concluded that Interior had breached its fiduciary duty in several respects: by failing to interpret correctly the royalty terms in the lease and regulations, by failing to insure that lessees comply with lease terms requiring diligent development, and by failing to insure the protection of leased lands from drainage. *Jicarilla Apache Tribe v. Supron Energy Corp.*, 479 F. Supp. 536, 547-51 (D.N.M. 1979). The trial court entered a declaratory judgment against the Secretary.[3] The majority opinion reverses the trial court's construction of the lease and the regulations, and finds it unnecessary to reach the other breach of trust issues. I disagree, and would affirm the trial court on each of these matters.

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held by Indians under allotment act trust patents. In *Poafpybitty v. Skelly Oil Co.*, 390 U.S. 365 (1968), the defendant lessee argued that the plaintiff Comanche Indians had no standing to sue under the lease because Interior "ha[d] such complete control over the lease that only [the Secretary could] institute . . . court action" for impairment of the Indians' interests under the lease. *Id.* at 372. The Court, noting that the government had exercised supervisory authority over oil and gas leases "in considerable detail," rejected the defendant's argument, holding that the Indians were not precluded thereby from bringing suit. *Id.* at 373. Concerning Interior's duties in the situation, the Court declared that "[i]f the Government does determine that there has been waste in violation of a lease, *it will of course satisfy its trust obligation* by filing the necessary court action." *Id.* (emphasis added).

[3] The Tribe has, of course, another remedy for the Government's breach of its fiduciary obligations. "If in carrying out [its] role as representative [of the Tribe], the Government violated its obligations to the Tribe, then the Tribe's remedy is against the Government . . . ." *Nevada v. United States*, 103 S.Ct. 2906, 2925 n.16 (1983) (Rehnquist, J.). That action lies in the Court of Claims. *See* 28 U.S.C. § 1505 (1976); *United States v. Mitchell (Mitchell II)*, 103 S.Ct. 2961, 2965 (1983). The Tribe has instituted a suit against the Government in the Court of Claims, which has been stayed pending this appeal.

A. *The Regulations*

The trial court stated the issue to be whether "the Secretary has breached his fiduciary duty because the method by which he computed royalties did not derive for the Tribe the highest royalties payable under the lease terms and the federal regulations." *Id.* at 549. The court then found that a breach had occurred. *Id.* at 551. The issue presented to us on appeal is one of interpretation of regulations, and not whether the Secretary was acting in accordance with his fiduciary obligations in promulgating the regulations initially.

At the time this litigation began, the Secretary used the BTU method to calculate royalties due the Tribe. One of the objectives sought by the Tribe was to compel Interior to calculate royalties using the net realization method as well, and to apply whichever method resulted in the greatest income to the Tribe. Sometime during the trial below, Interior evidently adopted the position that the lease and regulation terms authorized utilization of both methods of accounting (dual accounting), and that it has the discretion to require payment of royalties based on the method assuring the Tribe the highest return. *See* Rec., supp. vol. I, at 141-44.

On its cross-appeal to this court, Interior specifically "does not appeal the district court's holding that the 'dual accounting' method is the appropriate means of calculating royalties." Brief for the Secretary of the Interior at 9. Indeed, in its reply brief, Interior vigorously defends the trial court's holding on that issue against attack by defendant-lessees, concluding: "In short, the terms of the lease and the regulations grant the Secretary the authority to determine the value of the production at the lease on the basis of the value of the constituent commodities." Reply Brief for the Secretary of the Interior at 7. Moreover, the Secretary acknowledges his "broad discretion to determine the value

of production in the way he considers will best protect the royalty interest of the lessor." *Id.* at 10-11. Thus, the Secretary has adopted the view that interpreting the royalty terms to require dual accounting by the Jicarilla's lessees is reasonable. This interpretation is in accordance, so far as it goes, with the trial court's holding.

Without considering either Interior's current interpretation of its royalty provisions or its role as trustee, the majority disagrees with the trial court's interpretation and finds instead that dual accounting is not required under the regulations. The majority refuses to "set aside the Secretary's construction of his regulation and lease which was followed and applied without exception for these many years, a construction which has a perfectly reasonable basis in the lease and in the regulations." Slip op. at 9. It bases its opinion on the discretion granted the Secretary specifically by the lease terms and in "the regulation of oil and gas matters," because "the Secretary's interpretation was and is in conformance with the practices in the industry," and because the Secretary's action was not shown to be arbitrary or capricious. *Id.* The majority then states that "[w]hen the prevailing doctrine in this circuit is then applied to these circumstances we must conclude that the administrative interpretation . . . must be applied," *id.* at 10, adding that "[t]he Secretary's position is consistent with case law in this circuit. *See* Barby v. Cabot Corporation, 465 F.2d 11 (10th Cir.)," *id.*

I am at a loss to discern what the majority has in mind when it refers to "the prevailing doctrine in this circuit." Initially, I note that *Barby* dealt with the interpretation of lease terms entered into between two private parties and is therefore irrelevant to this case which involves the interpretation of federal regulations and fiduciary duties. I also do not see what relevance "industry practices" have to the Secretary's interpretation of federal law.

In my view, however, the most significant error the majority makes is its employment of administrative law analysis without considering what role, if any, the Secretary's fiduciary duty should play in a court's examination of his administrative action. As I have pointed out, the Secretary's actions in a situation such as this are constrained by principles of Indian trust obligations as well as by standards of administrative law.

The Supreme Court has implicitly recognized that stricter standards apply to federal agencies when administering Indian programs. *See Morton v. Ruiz*, 415 U.S. 199, 236 (1974); D. Getches, D. Rosenfelt & C. Wilkenson, Federal Indian Law 135-36 (1979). When the Secretary is acting in his fiduciary role rather than solely as a regulator and is faced with a decision for which there is more than one "reasonable" choice as that term is used in administrative law, he must choose the alternative that is in the best interests of the Indian tribe. In short, he cannot escape his role as trustee by donning the mantle of administrator, a principle recently made explicit by this court in *Jicarilla Apache Tribe v. Andrus*, 687 F.2d 1324 (10th Cir. 1982):

> "We are convinced . . . that the plain, mandatory terms of the regulations do not leave room for deference to this interpretation, which does not serve the interest of the Indians. If there is any doubt, the interpretation should be made liberally in favor of the Indians for whose protections these provisions were promulgated. *Antoine v. Washington*, 420 U.S. 194, 199, 200, 95 S.Ct. 944, 948, 43 L.Ed.2d 129; *Bryan v. Itasca County*, 426 U.S. 373, 392, 96 S.Ct. 2102, 2112, 48 L.Ed.2d 710. This rule of construction pertaining to statutes and treaties should also govern the interpretation of the regulations. Regulations are generally subject to the same rules of construction as statutes. *Rucker v. Wabash Railroad Co.*, 418 F.2d 146, 149 (7th Cir.)."

Id. at 1332.

Thus, the true issue in this case is not whether the Secretary's earlier application of the royalty terms was reasonable; rather, it is whether the alternative interpretion requiring dual accounting is also reasonable *and* better promotes the Tribe's interest. If so, dual accounting should have been required from the beginning.

Two sets of regulations and the lease terms are determinative of the Tribe's royalty claim. Title 25 and Title 30 of the C.F.R. each contain regulations addressing royalty calculations. The lease form at issue incorporates both sets of regulations by reference, and the royalty provision contained in the leases either quotes or paraphrases the relevant regulations printed in Title 25. Accordingly, the following discussion referring to both titles of the C.F.R. should be read as referring to the lease as well. The regulations at issue are reproduced in pertinent part in an appendix to this opinion.

The regulations contained in 25 C.F.R. require lessees to pay a royalty on the value or amount of all gas and other hydrocarbon substances produced from the lease.[4]

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[4] Natural gas is typically made up of several components in varying proportions. Generally, the gas at the wellhead consists of methane and ethane together with heavier components such as butane, propane, and natural gasoline. Where heavier components make up more than a standard percentage of the whole, the gas is called "wet" gas. When gas contains less than that percentage of heavier components, it is called "dry" gas. In the instant case, all of the gas produced from the tribal leases is wet gas.

Gas lessees may market wet gas in two ways. First, a lessee may choose to process the gas and market it separated into its constituent parts. The lessee does this by extracting the heavier components or "liquids" in a processing plant, and then selling the various products. Alternatively, the lessee may choose to sell the wet gas as is to a third party, who will then process the gas for further resale.

This case involves two methods of royalty calculations. The "BTU Method" calculates the value of gas produced by measuring the volume and BTU content of the wet gas at the wellhead, from which the "value" of the gas is derived. The second method, called

25 C.F.R. § 211.13 (1982) (formerly codified at 25 C.F.R. § 171.13). Section 211.13 contains a "favored nation clause" for calculating value: " 'value' . . . may . . . be calculated on the basis of the highest price paid or offered . . . at the time of production for the major portion of . . . gas . . . [and] all other hydrocarbon substances produced and sold from the field . . . . The actual amount realized by the lessee from the sale of said products may . . . be deemed mere evidence of or conclusive evidence of such value." *Id.* The regulation adds that the calculated value of products derived from treatment of gas should include an allowance for manufacturing costs. More importantly for the purposes of this case, however, the regulation states that "royalty will be computed on the value of gas or casing-head gas, or on the products thereof . . . *whichever is the greater.*" *Id.* (emphasis added).

Title 30 of the C.F.R. contains extensive provisions to be used in calculating royalties. The threshold regulation, cited by the majority, states that

> "(a) Royalty accrues on the dry gas, whether produced as such or as residue gas after the extraction of gasoline.
>
> "(b) If the lessee derives revenue on gas from two or more products, a royalty normally will be collected on all such products.

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the "net realization" or "aggregate value" method, is calculated by determining the values of the component gases after they have been extracted through processing. The "value" of the gas is the aggregate value of the constitutent gases, less a cost of processing allowance.

"Dual accounting," requiring the computation of the value of wet gas by both methods and the subsequent payment of royalties on the basis of whichever method yields the higher value, allows a lessee to market gas by whichever method it chooses and ensures that the lessor royalty holder receives the maximum return on its gas.

> "(c) For the purpose of computing royalty the value of wet gas shall be either the gross proceeds accruing to the lessee from the sale thereof or the aggregate value determined by the Secretary of all commodities, including residue gas, obtained therefrom, whichever is greater."

30 C.F.R. § 221.50 (1982). The second clause of subsection 221.50(c) authorizes Interior to use the aggregate value of the substances contained in wet gas, ensuring that the lessor will receive the true value of the gas and other hydrocarbons produced from its lands, regardless of the lessee's choice of marketing tactics. Subsection (c) does not by its terms require that the lessee itself extract liquids before the Secretary may utilize aggregate value computing; to the contrary, it appears to apply in *all* situations. By using the term "aggregate value," rather than "proceeds," the subsection allows the Secretary to use aggregate value in situations where the lessee does not in fact process wet gas or otherwise directly receive "proceeds" from the processing. The majority's interpretation ignores the distinction made in the regulation and, in fact, makes the first clause of subsection (c) irrelevant and redundant in light of subsection (b). The majority interprets subsection (c) to say in effect that when the lessee processes wet gas itself (and, presumably, sells the constituent products), the lessee must pay royalties on all the products—precisely what subsection (b) requires.

Moreover, practical considerations support this construction. The lessees argue that the dual accounting method of calculating royalties mandated by subsection 221.50(c) applies only when the lessees themselves extract the liquids from the wet gas and market the various products. They assert that dual accounting cannot be used when they merely sell unrefined wet gas to another company, because the other company is the one deriving the higher proceeds from the sales of the various deriva-

tive products. However, as I have stated, the purpose of the Indian Mineral Leasing Act is to ensure that Indian tribes receive the *maximum* benefit from mineral deposits on their lands, *see* slip op., dissent, at 6, and we should construe regulations enacted under this Act in light of this purpose. *Trustees of Indiana University v. United States*, 618 F.2d 736, 739 (Ct. Cl. 1980); *Alaska Interstate Co. v. McMillian*, 402 F.Supp. 532, 555 (D. Del. 1975); *see also Jicarilla Apache Tribe v. Andrus*, 687 F.2d 1324, 1332 (10th Cir. 1982) (regulations generally subject to same rules of construction as statutes).

Adopting the lessee's construction of the regulations would too easily enable lessees of Indian oil and gas leases to avoid the purpose of the Act. If the value of wet gas is increased by processing, it is in every lessees' best interest to have their royalty payments calculated on the value of unrefined wet gas, rather than on the aggregate value of the various products. Under the lessee's construction, to obtain the advantage of royalties calculated on the lower, wellhead price, all a lessee need do is sell the unprocessed wet gas to a cooperative third party, pay the lower royalties, and then reap the benefits of the higher proceeds from the extracted products through a sweetheart deal with the third party. In my view, it is as "reasonable" to construe these regulations in a way that prevents easy avoidance of the clear congressional intent of the Act as it is to adopt the majority's position.

The regulations thus provide support for the position urged by the Secretary on appeal. As I have noted, our initial determination is whether the trial court's and the Secretary's construction of the royalty regulations is reasonable. I believe that it is. Given two reasonable interpretations, Interior's trust responsibilities require it to apply whichever accounting method (BTU or net realization) yields the Tribe the greatest royalties. I would affirm the trial court on this point.

B. *The Secretary's Administration of the Leases*

The trial court found that the defendant-lessees had not failed to diligently develop the leases in question. Nonetheless, the trial court found that fact fortuitous because the Secretary had "failed to adequately monitor development of these leases sufficiently to insure compliance with the terms thereof," thereby breaching his fiduciary duty to the Tribe. 479 F. Supp. at 547. Similarly, the trial court found that there was no drainage, but concluded that the Secretary had been negligent in monitoring the potential problem, and thus had breached his fiduciary duties. *Id* at 548.

The record supports the trial court's findings on both of these issues, and I would affirm.

III.

PREEMPTION

By order issued January 26, 1981, the district court held that the New Mexico Natural Gas Pricing Act does not apply either to sale prices received by lessees, or to royalties received by the Tribe. The majority disagrees, holding that the NMNGPA applies to both, even though it "is a limit on the size of the royalty owner's check." Slip op. at 15. The majority acknowledges that "[t]here is by reason of the state price control act an effect on the money the tribe receives from the sales," but concludes that this harmful aspect of state regulation is permissible because "there is no direct conflict with Indian self-government," *id.* at 16.

Initially, I note that the State disagrees with the majority's viewpoint concerning tribal royalties. The State argues that the Act's price ceilings will not necessarily affect the Tribe's royalties, because royalties need not be limited to proceeds received by the lessees.[5] *See*

[5] Interior also argues that value for royalty purposes can exceed governmentally imposed price ceilings. Reply Brief for the Secretary of the Interior at 8-12.

Brief of Cross-Appellant State of New Mexico at 56-58. This argument is in line with my construction of the federal regulations. In the State's view, the trial court correctly held that value for royalty purposes can exceed sale prices, and thus can exceed the price limits established by the NMNGPA. Indeed, the NMNGPA itself provides that the maximum allowable base prices established by the Act for natural gas "shall be exclusive of, . . . if provided for by contract, that portion of royalty payable on a value in excess of the contract sales price." N.M. Stat. Ann. § 62-7-3 (1982). Thus, in future contracts the Tribe can clearly avoid any effect upon its royalties by the Act. By implication, however, the Act might be interpreted to limit tribal royalties when *not* expressly avoided by contract terms, as in this case. I reject this conclusion for the reasons set forth in this opinion.

The majority's analysis of the effect of the New Mexico Act on "Indian self-government" relies upon a mistaken view of the significance of *Washington v. Confederated Tribes of the Colville Indian Reservation*, 447 U.S. 134 (1980), and *Moe v. Confederated Salish & Kootenai Tribes*, 425 U.S. 463 (1976), which it cites as dispositive of this issue. I disagree both with the majority's analysis and with its reliance on *Confederated Tribes* and *Moe*. My analysis is limited to the question whether federal law preempts the State from placing a ceiling on royalties paid to Indians. I need not address whether the NMNGPA may properly apply a ceiling on the sale of gas produced from the reservation by non-Indian lessees, because even if such a ceiling is appropriate it would not limit the determination of the Tribe's royalties under my construction of the regulations.

The Indian Mineral Leasing Act guarantees to Indian tribes maximum royalties from oil and natural gas located on tribal lands. In spite of clear congressional intent to ensure that Indian tribes receive the maximum

return from their natural resources by way of royalties, the majority holds that a state can frustrate that policy. I would hold to the contrary, because I believe that the New Mexico Act is preempted by federal law to the extent that it adversely affects tribal oil and gas royalties.

The Supreme Court has recently discussed at length the principles to be used in determining whether a state civil statute is applicable within a reservation. *See White Mountain Apache Tribe v. Bracker*, 448 U.S. 136, 141-45 (1980). In pertinent part, the Court noted that

> "[There are] two independent but related barriers to the assertion of state regulatory authority over tribal reservations and members. First, the exercise of such authority may be pre-empted by federal law. . . . Second, it may unlawfully infringe 'on the right of reservation Indians to make their own laws and be ruled by them.' . . . The two barriers are independent because either, standing alone, can be a sufficient basis for holding state law inapplicable to activity undertaken on the reservation or by tribal members. . . .
>
> "The unique historical origins of tribal sovereignty make it generally unhelpful to apply to federal enactments regulating Indian tribes those standards of pre-emption that have emerged in other areas of the law. Tribal reservations are not States, and the differences in the form and nature of their sovereignty make it treacherous to import to one notions of pre-emption that are properly applied to the other. The tradition of Indian sovereignty over the reservation and tribal members must inform the determination whether the exercise of state authority has been pre-empted by operation of federal law. . . . As we have repeatedly recognized, this tradition is reflected and encouraged in a number of congressional enactments demonstrating a firm federal policy of pro-

> moting tribal self-sufficiency and economic development. Ambiguities in federal law have been construed generously in order to comport with these traditional notions of sovereignty and with the federal policy of encouraging tribal independence. . . . We have thus rejected the proposition that in order to find a particular state law to have been preempted by operation of federal law, an express congressional statement to that effect is required. . . . At the same time any applicable regulatory interest of the State must be given weight, . . . and 'automatic exemptions "as a matter of constitutional law" ' are unusual."

Id. at 142-44.

As *White Mountain Apache Tribe v. Bracker* makes clear, whether a state law interferes with Indian self-government is only half of the appropriate analysis.[6] The state law in question must also be examined for possible conflict with federal law. The Supreme Court has recently pointed out that the special doctrine of Indian preemption referred to in *White Mountain Apache Tribe v. Bracker* is considerably *broader* than other, more familiar forms of preemption. *See New Mexico v. Mescalero Apache Tribe*, 103 S.Ct. 2378, 2386 (1983). State law and jurisdiction are preempted by operation

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[6] The majority's reliance upon *Montana v. United States*, 450 U.S. 544 (1980), is also misplaced. That case involved very narrow questions of tribal sovereignty and regulatory authority that are not present in this case. As the Court itself noted, "the regulatory issue before us is a narrow one . . . the question of the power of the Tribe to regulate non-Indian fishing and hunting on reservation land owned in fee by nonmembers of the Tribe." *Id.* at 557. The Tribe is not asserting regulatory authority in this case. Additionally, the significance of a tribal land-base (lacking in *Montana*) to questions of a tribe's sovereign authority has been noted repeatedly by courts and commentators. *See, e.g., New Mexico v. Mescalero Apache Tribe*, 103 S.Ct. 2378, 2384 (1983). Accordingly, general principles of tribal sovereignty applicable to tribal authority over tribal land should not be extrapolated from *Montana*, a narrow, fact-bound case.

of federal law if they interfere with or are incompatible with federal and tribal interests reflected in federal law,[7] unless the state interests at stake are sufficient to justify the effect. *Id.* Without addressing the Indian self-government issue, I would hold that to the extent the state law is interpreted to place a ceiling on the Tribe's royalties, it conflicts impermissibly with federal law.

The Supreme Court has emphasized the existence of a "firm federal policy of promoting tribal self-sufficiency and economic development." *White Mountain Apache Tribe v. Bracker*, 448 U.S. at 143; *see also New Mexico v. Mescalero Apache Tribe*, 103 S.Ct. at 2386-87. This policy is demonstrated by federal statutes authorizing the sale of tribal resources for the tribes' benefit, such as the Indian Mineral Leasing Act. *See id.* at 2387; *see also White Mountain Apache Tribe v. Bracker*, 448 U.S. at 143 & n.10. The right to receive maximum royalties is a benefit granted by Congress to the tribes in the Leasing Act. The state law here imposes a maximum price ceiling lower than the federal ceiling on sales of gas by non-Indian lessees, and thus could operate to decrease tribal royalties. This result would interfere with the congressional policy embodied in the Indian Mineral Leasing Act.

It is therefore clear to me that the New Mexico Act is preempted by operation of federal law insofar as it has any harmful effect upon the Tribe's royalty revenue, unless sufficient state interests are at stake. The State points to no on-reservation actions by it justifying this intrusion. *See id.* at 2387, 2390-91; *White Mountain Apache Tribe v. Bracker*, 448 U.S. at 150-51. In fact, as I have pointed out, New Mexico has conceded in this case that its ceilings on gas sales do not limit royalties. Nevertheless, the lessees assert that the State's justifica-

[7] Congress need not make any explicit statement for state law to be preempted in this context. *White Mountain Apache Tribe v. Bracker*, 448 U.S. 136, 144, 150-51 (1980).

tion for imposition of state price ceilings on gas *sales* by non-Indian lessees (that such price controls are necessary for the benefit of natural gas consumers) also justifies a comparable ceiling on tribal royalties under current contracts. The record contains no showing that the lack of a ceiling on royalties paid to Indians in New Mexico would have such a significant effect upon New Mexico consumers that imposition of the Act to limit royalties would be of vital interest to the State.

I conclude that the New Mexico Act is preempted under the principles enunciated in *White Mountain Apache Tribe v. Bracker* insofar as it might be applied to limit royalties received by the Tribe. The cases relied on by the majority are inapposite. The enterprise here—the production of reservation oil and gas—is far removed from those involved in *Confederated Tribes* and *Moe*, where the tribal contributions to the enterprises were "de minimus," *New Mexico v. Mescalero Apache Tribe*, 103 S.Ct. at 2390, and the product marketed was not generated from reservation resources, *compare Confederated Tribes* and *Moe with White Mountain Apache Tribe v. Bracker*. To the contrary, the production of tribal oil and gas clearly involves " 'value generated on the reservation by activities involving the Trib[e],' " *New Mexico v. Mescalero Apache Tribe*, 103 S.Ct. at 2390 (quoting *Confederated Tribes*, 447 U.S. at 156-57), and thus is protected from state interference.

The majority accepts the proposition that Congress delegated to the states the authority to regulate gas prices, and thus royalties, of gas produced on Indian reservations and sold intrastate. Far from being compelled, in my view this conclusion is belied both by the language of the Natural Gas Policy Act of 1978, 15 U.S.C. §§ 3311-3432 (Supp. V 1981) (NGPA) and by our prior caselaw.

The NGPA provides in a section entitled "Effect on State laws":

> "Nothing in this chapter shall affect the authority of any State to establish or enforce any maximum lawful price for the first sale of natural gas produced in such State which does not exceed the applicable maximum lawful price, if any, under subchapter I of this chapter."

Id. § 3432(a). The power to regulate on Indian reservations has always resided in the federal government. That power can only be delegated by express language.

> "As this court has recently emphasized, '[T]he cases stress that *regulatory* powers in Indian country or on Indian lands belong to the Congress except for inherent jurisdiction of the tribes. Congress may delegate this authority to the state, but when it does so it must be in specific terms.' "

Mescalero Apache Tribe v. New Mexico, 630 F.2d 724, 730 (10th Cir. 1980) (quoting *United States v. New Mexico*, 590 F.2d 323, 328 (10th Cir. 1978), *cert. denied*, 444 U.S. 832 (1979) (emphasis added)), *vacated and remanded*, 450 U.S. 1036 (1981), *aff'd*, 677 F.2d 55 (10th Cir. 1982), *aff'd*, 103 S.Ct. 2378 (1983); *see, e.g.*, *Bryan v. Itasca County*, 426 U.S. 373, 392 (1976); *Donovan v. Navajo Forest Products Industries*, 692 F.2d 709, 711, 713 (10th Cir. 1982). Section 3432(a) does not refer to Indian reservations, and clearly grants no authority to the states to regulate on-reservation activities. Absent a specific statement of congressional intent, it cannot represent congressional authorization for New Mexico to override the benefits conferred to the Indian tribes in the Indian Mineral Leasing Act.[8]

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[8] The lessees argue that part of the legislative history of the National Gas Policy Act of 1978, 15 U.S.C. §§ 3311-3432 (Supp. V 1981) (NGPA), supports their delegation-of-authority argument. The Conference Report on the NGPA states:

> "The conference agreement provides that nothing in this Act shall affect the authority of any State to establish or enforce

Even assuming that New Mexico has authority to regulate the sale price of gas sold by non-Indian lessees of Indian reservation leases, an issue that I have not reached, I conclude that Congress did not delegate to the states authority to place ceilings on the royalties the tribes are entitled to receive from such leases. Constitutionally, the New Mexico Act may not be permitted to affect the amount of royalties received by the Jicarilla Apache Tribe. The Secretary should not consider himself limited by wellhead prices conforming to the Act when establishing "value" for the purpose of computing tribal royalties.

IV.

ANTITRUST

In discussing section 8 of the Clayton Act, 15 U.S.C. § 19 (1981), the majority opinion employs a rule of reason analysis to determine whether the existence of interlocking directors in violation of the Act is illegal. The few courts and authorities that have considered the issue have held that conduct violative of section 8 is illegal *per se*. *See, e.g., Protectoseal Co. v. Baracek*, 484 F.2d 585, 589 (7th Cir. 1973); P. Areeda, *Antitrust Analysis* ¶ 666 (3d ed. 1981); 4 Von Kalinowski, *Antitrust Laws and Trade Regulation* § 21.02 [2]. It seems

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any maximum lawful price for sales of gas in intrastate commerce which does not exceed the applicable maximum lawful price, if any, under Title I of this Act. This authority extends to the operation of any indefinite price escalator clause. The Congress enacts this provision with a recognition that it is ceding its authority under the commerce clause of the Constitution to regulate prices for such production to affected States."

H.R. Conf. Rep. No. 1752, 95th Cong., 2d Sess. 124-25, *reprinted in* 1978 U.S. Code Cong. & Ad. News 8983, 9041. The first sentence of this discussion confirms the clear language of the statute. The last sentence is apparently at variance with the enacted language. As stated in text, Congress' power to regulate Indian affairs can only be delegated expressly.

to me that if an interlocking directorate falls within section 8, which is very specific, the interlock is unlawful and no rule of reason analysis is necessary. Because the purpose of section 8 is to nip antitrust violations in the bud, *TRW Inc. v. FTC*, 647 F.2d 942, 946-47 (9th Cir. 1981), injunctive relief for such a violation without proof of actual anticompetitive effect should be available under 15 U.S.C. § 26 (1982) to protect "against *threatened* loss or damage by a violation." *Id.* (emphasis added).

In this case, however, plaintiff is seeking treble damages under section 4 of the Clayton Act, 15 U.S.C. § 15 (1982), which requires "some showing of *actual injury* attributable to something the antitrust laws were designed to prevent." *J. Truett Payne Co. v. Chrysler Motors*, 451 U.S. 557, 562 (1981) (emphasis added). Because I agree with the majority's conclusion that plaintiff here has failed to make the requisite showing of damage under section 4, I would affirm the district court on that basis only.

APPENDIX

Pertinent Regulations

25 C.F.R. pt. 211, Bureau of Indian Affairs (1982).

"§ 211.13 Rates of rentals and royalties under oil and gas leases.

"(a) The lessee shall pay . . . a rental of $1.25 per acre per annum in advance during the continuance thereof, together with a royalty of 12½ percent or the value of amount of all oil, gas, and/or natural gasoline, and/or all other hydrocarbon substances produced and saved from the land leased, save and except oil, and/or gas used by the lessee for development and operation purposes on the lease, which oil or gas shall be royalty free. . . . During the period of supervision, 'value' for the purposes of the lease may, in the discretion of the Secretary of the Interior, be calculated on the basis of the highest price paid or offered (whether calculated on the basis of short or actual volume) at the time of production for the major portion of the oil of the same gravity, and gas, and/or natural gasoline, and/or all other hydrocarbon substances produced and sold from the field where the leased lands are situated, and the actual volume of the marketable product less the content of foreign substances as determined by the supervisor. The actual amount realized by the lessee from the sale of said products may, in the discretion of the Secretary of the Interior, be deemed mere evidence of or conclusive evidence of such value. . . . In determining the value for royalty purposes of products, such as natural gasoline, that are derived from treatment of gas, a reasonable allowance for the cost of manufacture shall be made, such allowance to be two-thirds of the value of the marketable product unless otherwise determined by

the Secretary of the Interior on application of the lessee or on his own initiative, and that royalty will be computed on the value of gas or casing-head gas, or on the products thereof (such as residue gas, natural gasoline, propane, butane, etc.), whichever is the greater."

. . . .

"§ 211.21 Restrictions on operations.

"(a) Oil and gas leases issued under the provisions of the regulations in this part shall be subject to imposition by the Secretary of the Interior of such restrictions as to time or times for the drilling of wells and as to the production from any well or wells as in his judgment may be necessary or proper for the protection of the natural resources of the leased land and in the interest of the lessor. In the exercise of his judgment the Secretary of the Interior may take into consideration, among other things, the Federal laws, State laws, regulations by competent Federal or State authorities, lawful agreements among operators regulating either drilling or production, or both, and any regulatory action desired by tribal authorities."

30 C.F.R. pt. 221, Minerals Management Service (1982).

"§ 221.46 Quality basis for computing royalties on natural gasoline, butane, propane, and other liquid hydrocarbon substances extracted from gas.

"(a) If the net output of a plant is derived from the gas obtained from only one leasehold, the quantity of gasoline or other liquid hydrocarbon substances of which computations of royalty for the lease are based is the net output of the plant.

"(e) The supervisor is authorized, whenever in his judgment neither method prescribed in para-

graph (b) and (c) of this section is practicable, to estimate the production of natural gasoline, butane, propane, or other liquid hydrocarbon substances from any leasehold from: (1) The quantity of gas produced from the leasehold and transmitted to the extraction plant, (2) the gasoline, butane, propane, or other liquid hydrocarbon content of such gas as determined by test, and (3) a factor based on plant efficiency or recovery and so determined as to insure full protection of the royalty interest of the lessor."

"§ 221.47 Value basis for computing royalties.

"The value of production, for the purpose of computing royalty shall be the estimated reasonable value of the product as determined by the supervisor, due consideration being given to the highest price paid for a part or for a majority of production of like quality in the same field, to the price received by the lessee, to posted prices and to other relevant matters. Under no circumstances shall the value of production of any of said substances for the purposes of computing royalty be deemed to be less than the gross proceeds accruing to the lessee from the sale thereof or less than the value computed on such reasonable unit value as shall have been determined by the Secretary. In the absence of good reason to the contrary, value computed on the basis of the highest price per barrel, thousand cubic feet, or gallon paid or offered at the time of production in a fair and open market for the major portion of like-quality oil, gas, or other products produced and sold from the field or area where the leased lands are situated will be considered to be a reasonable value."

"§ 221.50 Royalty on gas.

"The royalty on gas shall be the percentage established by the terms of the lease of the value or amount of the gas produced.

"(a) Royalty accrues on dry gas, whether produced as such or as residue gas after the extraction of gasoline.

. . . .

"(c) For the purpose of computing royalty the value of wet gas shall be either the gross proceeds accruing to the lessee from the sale thereof or the aggregate value determined by the Secretary of all commodities, including residue gas, obtained therefrom, whichever is greater."

"§ 221.51 Royalty on casing-head or natural gasoline, butane, propane, or other liquid hydrocarbon substances extracted from gas.

"A royalty as provided in the lease shall be paid on the value of one-third (or the lessee's portion if greater than one-third) of all casing-head or natural gasoline, butane, propane, or other liquid hydrocarbon substances extracted from the gas produced from the leasehold. The value of the remainder is an allowance for the cost of manufacture, and no royalty thereon is required. The value shall be so determined that the minimum royalty accruing to the lessor shall be the percentage established by the lease of the amount or value of all extracted hydrocarbon substances accruing to the lessee under an arrangement, by contract or otherwise, for extraction and sale that has been approved by the supervisor."

Pertinent Lease Terms

Lease Form No. 157, Oil and Gas Mining Lease—Tribal Indian Lands.

"3. In consideration of the foregoing, the lessee hereby agrees:

"(a) Bond.—To furnish such bond as may be required by the regulations of the Secretary of the

Interior, with satisfactory surety, or United States bonds as surety therefor, conditioned upon compliance with the terms of this lease.

"(b) Wells—(1) To drill and produce all wells necessary to offset or protect the leased land from drainage or in lieu thereof, to compensate the lessor in full each month for the estimated loss of royalty through drainage; *Provided*, That during the period of supervision by the Secretary of the Interior, the necessity for offset wells shall be determined by the oil and gas supervisor and payment in lieu of drilling and production shall be with the consent of, and in an amount determined by the Secretary of the Interior; (2) at the election of the lessee to drill and produce other wells; *Provided*, That the right to drill and produce such other wells shall be subject to any system of well spacing or production allotments authorized and approved under applicable law or regulations, approved by the Secretary of the Interior and affecting the field or area in which the leased lands are situated; and (3) if the lessee elects not to drill and produce such other wells for any period the Secretary of the Interior may, within 10 days after due notice in writing, either require the drilling and production of such wells to the number necessary, in his opinion, to insure reasonable diligence in the development and operation of the property, or may in lieu of such additional diligent drilling and production require the payment on and after the first anniversary date of this lease of not to exceed $1 per acre per annum, which sum shall be in addition to any rental or royalty hereinafter specified.

"(c) Rental and royalty.—To pay, beginning with the date of approval of the lease by the Secretary of the Interior or his duly authorized representative, a rental of $1.25 per acre per annum in advance dur-

ing the continuance hereof, the rental so paid for any one year to be credited on the royalty for that year, together with a royalty of 16⅔ percent of the value or amount of all oil, gas and/or natural gasoline, and/or all other hydrocarbon substances produced and saved from the land leased herein, save and except oil, and/or gas used by the lessee for development and operation purposes on said lease, which oil or gas shall be royalty free. During the period of supervision, "value" for the purposes hereof may, in the discretion of the Secretary, be calculated on the basis of the highest price paid or offered (whether calculated on the basis of short or actual volume) at the time of production for the major portion of the oil of the same gravity, and gas and/or natural gasoline, and/or all other hydrocarbon substances produced and sold from the field where the leased lands are situated, and the actual volume of the marketable product less the content of foreign substances as determined by the oil and gas supervisor. The actual amount realized by the lessee from the sale of said products may, in the discretion of the Secretary, be deemed mere evidence of or conclusive evidence of such value. When paid in value, such royalties shall be due and payable monthly on the last day of the calendar month following the calendar month in which produced, when royalty on oil produced is paid in kind, such royalty oil shall be delivered in tanks provided by the lessee on the premises where produced without cost to the lessor unless otherwise agreed to by the parties thereto, at such time as may be required by the lessor; *Provided*, That the lessee shall not be required to hold such royalty oil in storage longer than 30 days after the end of the calendar month in which said oil is produced; *And provided further*, That the lessee shall be in no manner responsible or held liable for loss or destruction of such oil in

storage caused by acts of God. All rental and royalty payments, except as provided in section 4(c) shall be made by check or draft drawn on a solvent bank, open for the transaction of business on the day the check or draft is issued, to the payee designated by the Area Director. All such rental and royalty payments shall be mailed to the oil and gas supervisor for transmittal to the payee designated by the Area Director. It is understood that in determining the value for royalty purposes of products, such as natural gasoline, that are derived from treatment of gas, a reasonable allowance for the cost of manufacture shall be made, such allowance to be two-thirds of the value of the marketable product unless otherwise determined by the Secretary of the Interior on application of the lessee or on his own initiative, and that royalty will be computed on the value of gas or casinghead gas, or on the products thereof (such as residue gas, natural gasoline, propane, butane, etc.), whichever is the greater.

. . . .

"(f) Diligence, prevention of waste.—To exercise reasonable diligence in drilling and operating wells for oil and gas on the lands covered hereby, while such products can be secured in paying quantities; to carry on all operations hereunder in a good and workmanlike manner in accordance with approved methods and practice, having due regard for the prevention of waste of oil or gas developed on the land, or the entrance of water through wells drilled by the lessee to the productive sands or oil or gas-bearing strata to the destruction or injury of the oil or gas deposits, the preservation and conservation of the property for future productive operations, and to the health and safety of workmen and employees; to plug securely all wells before abandoning the same and to effectually shut off water from the

oil or gas-bearing strata; not to drill any well within 200 feet of any house or barn now on the premises without the lessor's written consent; to carry out at the expense of the lessee all reasonable orders and requirements of the oil and gas supervisor relative to prevention of waste, and preservation of the property and the health and safety of workmen; to bury all pipe lines crossing tillable lands below plow depth unless other arrangements therefor are made with the superintendent; to pay the lessor all damages to crops, buildings, and other improvements of the lessor occasioned by the lessee's operations; *Provided*, That the lessee shall not be held responsible for delays or casualties occasioned by causes beyond the lessee's control."

Rec., jt. app. vol. I, at 13-15.

APPENDIX C

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF NEW MEXICO

No. 75-247-M Civil

JICARILLA APACHE TRIBE,
Plaintiff,

v.

SOUTHERN UNION GAS COMPANY, *et al.*,
Defendants.

[Filed Sept. 7, 1978]

MEMORANDUM OPINION

This matter came up on cross motions for partial summary judgment by the plaintiff and all remaining defendants, and having considered said motions, and the memoranda of counsel, affidavits, depositions and exhibits, the following opinion will dispose of the points raised by the parties.

POINT I

Plaintiff alleges that the defendants have not calculated royalties on the "value" of natural gas, oil and liquid hydrocarbon substances as required by the leases involved herein. I conclude, however, that as a matter of law the "value" was determined by the Secretary of the Interior (Secretary), and that retroactive reassessment of the value is improper. The defendants' motions for partial summary judgment as to this issue should

be granted, as all parties agree and I find that there is no issue of material fact which would necessitate a trial on this issue.

The essence of plaintiff's claim is that the Secretary did not determine "value" prior to the institution of this lawsuit as that term is defined in the leases and that this Court should determine "value" after an evidentiary hearing or order the Secretary to do so. The Secretary has in fact already determined "value" for royalty purposes in accordance with the terms of the leases and regulations, and the plaintiff disagrees with this determination.

The leases are Standard Form 157 Department of Interior lease forms, paragraph 3(c) of which defines the term "value":

> During the period of supervision, "value" for the purposes hereof may, in the discretion of the Secretary, be calculated on the basis of the highest price paid or offered (whether calculated on the basis of short or actual volume) at the time of production for the major portion of the oil of the same gravity, and gas, and/or natural gasoline, and/or all other hydrocarbon substances produced and sold from the field where the leased lands are situated, and the actual volume of the marketable product less the content of foreign substances as determined by the oil and gas supervisor. The actual amount realized by the lessee from the sale of said products may, in the discretion of the Secretary, be deemed mere evidence of or conclusive evidence of such value.

Certain provisions of 30 CFR are made applicable by the leases to the determination of value on which royalties are based. 30 CFR 221.47 provides:

> The value of production, for the purpose of computing royalty shall be the estimated reasonable value of the product as determined by the Supervisor, due

> consideration being given to the highest price paid for a part or for a majority of production of like quality in the same field, to the price received by the lessee, to posted prices and to other relevant matters. Under no circumstances shall the value of production of any of said substances for the purposes of computing royalty be deemed to be less than the gross proceeds accruing to the lessee from the sale thereof or less than the value computed on such reasonable unit value as shall have been determined by the Secretary. In the absence of good reason to the contrary, value computed on the basis of highest price per barrel, thousand cubic feet, or gallon paid or offered at the time of production in a fair and open market for the major portion of like-quality oil, gas, or other products produced and sold from the field or area where the leased lands are situated will be considered to be reasonable value.

Royalties have been paid by all defendants based upon a determination and billing by the Secretary. The defendants filed regular monthly Statements of Oil and Gas Runs and Royalties on each of the leases. The value for royalty purposes shown in these monthly statements were the sales prices received by defendants at the wellhead. The Secretary, through the United States Geological Survey (USGS) issued monthly billings of royalties to the defendants based upon these wellhead sales prices received by the defendants. This was an exercise of the Secretary's discretion based upon the regulations and the leases, whereby he conclusively established value for royalty purposes as the sale price received at the wellhead. The rendition of these statements and billings by the USGS constitutes an official act of the Secretary. 25 CFR 171.13.

This determination by the Secretary may be challenged in an administrative appeal, and this court would then be able to review the agency action under 5 USC

706. However, the plaintiff did not exhaust this administrative remedy, and failed to provide the Secretary with "good reason" to compute "value" differently. In addition, the plaintiff has failed to allege any arbitrary, capricious or unlawful actions, or abuse of discretion by the Secretary.

In *Continental Oil Co. v. United States*, 184 F.2d 802 (Tenth Cir. 1950), the court specifically held that determinations of value for royalty payments could not be applied retrospectively to recompute gas royalties. I conclude therefore, that plaintiff's request that this Court redetermine the "value" for royalty purposes for years past, where billings have been made and royalties have been paid, would be improper.

Point II

The plaintiff alleges that the leases involved herein require the defendants to account for liquid hydrocarbon substances in the natural gas stream by both the net realization method and the BTU adjustment method, and that royalties should be paid on the basis of whichever accounting method creates the greater revenue. In December, 1976, the Secretary of the Interior directed Southern Union Gas Company to make a duel accounting for plaintiff's liquid hydrocarbon substances, as plaintiff has requested herein; the Secretary's decision is being appealed, and the determination upon appeal may well dispose of this issue, subject to possible review here. I therefore conclude that a ruling here on this issue should be deferred until such time as the appeal is complete, unless it appears that the disposition upon appeal has been unreasonably delayed.

POINT III

The plaintiff asserts that there is no genuine issue of material fact and that as a matter of law it is entitled to have the cost of manufacture allowance, which has

been determined by the Secretary, implemented and used in accounting for liquids by the net realization method of accounting. The resolution of this issue, however, is necessarily contingent upon the determination of Point II above, which has been reserved until the conclusion of the appeal process. Ruling on this issue will therefore be deferred until such time as Point II is again before this court for adjudication.

Point IV

The plaintiff has requested partial summary judgment granting the relief prayed for in paragraphs 2, 4, and 5 of the prayer for relief of the Fourth Cause of Action of the Amended Complaint. As to the claim for dual accounting for liquids, this issue has been deferred until the appeal process is complete (see Point II above). On the issue of the value of natural gas, oil and liquids for royalty purposes, the plaintiff's motion for summary judgment should be denied and the defendants' motions granted on the basis of the law set forth in Point I above.

The plaintiff has further alleged that the defendants are required by the leases to drill offset wells or alternatively that defendants' rights in the spacing units of each case where offset wells should have been drilled be cancelled. In addition, the plaintiff alleges that the defendants must, as a matter of law, explore and develop plaintiff's lands to the fullest extent possible, or suffer cancellation of their leases as to any undeveloped geological formations. Paragraph 3(b) of the leases requires the defendants to:

> drill and produce all wells necessary to offset or protect the leased lands from drainage [by wells on adjoining lands not the property of the lessor] or in lieu thereof, to compensate the lessor in full each month for the estimated loss of royalty through drainage . . . if the lessee elects not to drill and

> produce such other wells for any period the Secretary of the Interior may, within 10 days after due notice in writing, either require the drilling and production of such wells to the number necessary, in his opinion, to insure reasonable diligence in the development of the property, or may, in lieu of such additional diligent drilling and production, require the payment on and after the first anniversary date of this lease of not to exceed $1 per acre per annum, which sum shall be in addition to any rental or royalty hereinafter specified.

It is not clear whether the bracketed language appears in paragraph 3(b) of the leases involved herein. A review of the record indicates that there are outstanding questions of material fact which make summary judgment improper at this point. However, the determination of these outstanding questions of fact should be made in the first instance by the Secretary of the Interior, as is provided for in the leases in this case. *Pan American Petroleum Corp. v. Udall*, 192 F.Supp 626 (D.D.C. 1961). Ruling on this issue will therefore be deferred for a period of 120 days so that the Secretary will have the opportunity to determine whether offset wells are necessary; whether there has been a failure to develop; whether the leases limit the necessity for offset wells to drainage "by wells on adjoining lands not the property of the lessor" or whether there is a duty to drill offset wells on lands owned by the plaintiff; which leases have not been diligently developed in each geological formation; whether additional development wells can and should be drilled which will probably produce a profit for the defendants and which are necessary to insure "reasonable diligence in the operation of the property"; and whether cancellation is required of defendants' rights to undeveloped geological formations or spacing units where offset wells should have been drilled. The Secretary should make these determinations and issue direc-

tives in accordance with his authority under the leases and the law, subject to review by this court. If the Secretary has failed to make such determinations within 120 days, these issues will be resolved after a full hearing on the merits.

An order will be entered consistent with this Opinion.

/s/ E. L. Mechem
United States District Judge

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF NEW MEXICO

No. 75-246-M Civil

JICARILLA APACHE TRIBE,
Plaintiff,

v.

SOUTHERN UNION GAS COMPANY, *et al.*,
Defendants.

[Filed Sept. 7. 1978]

ORDER

This matter having come up on cross-motions for summary judgment by the plaintiff and the remaining defendants herein, and a memorandum opinion having been entered constituting the findings of fact and conclusions of law in this case; Now, Therefore,

IT IS ORDERED that the plaintiff's motion for summary judgment as to the issue of "value" for royalty purposes is hereby denied and the defendants' motions for summary judgment on this same issue are hereby granted;

IT IS FURTHER ORDERED that a ruling on the issue of dual accounting, the cost of manufacture allowance, and the relief prayed for in paragraph two of the prayer for relief of the Fourth Cause of Action of the Amended Complaint is hereby deferred until the administrative appeal on the issue of dual accounting is complete, unless there is unreasonable delay in the disposition of this appeal;

IT IS FURTHER ORDERED that as to paragraph four of the prayer for relief of the Fourth Cause of Action of the Amended Complaint, summary judgment in favor of the defendants is hereby granted and the plaintiff's motion for summary judgment is hereby denied;

IT IS FURTHER ORDERED that as to paragraph five of the prayer for relief of the Fourth Cause of Action of the Amended Complaint, the issue of offset wells and diligent development of the property, are hereby remanded to the Secretary of Interior for a period of 120 days for his determination of all facts and necessary or relevant issues which will enable him to issue directives consistent with his authority under the law, leases and regulations applicable herein, subject to review by this court.

/s/ E. L. Mechem
United States District Judge

APPENDIX D

IN THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF NEW MEXICO

No. 75-247-M Civil

THE JICARILLA APACHE TRIBE,
Plaintiff,

vs.

SOUTHERN UNION GAS CO., *et al.*,
Defendants.

[Filed Dec. 19, 1978]

MEMORANDUM OPINION AND ORDER

This matter comes up for consideration on plaintiff's motions to revise the Memorandum Opinion and Order filed September 7, 1978, and for leave to file a Second Amended Complaint. That portion of the Memorandum Opinion and Order of which plaintiff seeks revision granted summary judgment to defendants on the issue of whether the Secretary of Interior has determined "value" for royalty purposes in accordance with the terms of the leases and applicable federal regulations. I conclude in that Opinion that royalties have been paid by defendants "based upon a determination and billing by the Secretary," that "value for royalty purposes . . . were [sic] the sales prices received by defendants at the wellhead," that "[t]he Secretary, through the United States Geological Survey (USGS) issued monthly billings or royalties to the defendants based upon these wellhead sales

prices . . . ," and "[t]his was an exercise of the Secretary's discretion . . . ."

Plaintiff, in its Motion to Revise, suggests that I am uninformed as to the actual import of the monthly Statements of Account filed by defendants with the USGS and on which I have concluded the Secretary bases his determination of "value" for royalty purposes. Plaintiff further suggests that contrary to the language of the Memorandum Opinion, no appeal can be taken from the Secretary's billing procedure as described above.

Plaintiff argues that the monthly Statements of Account cannot possibly be construed as billings for royalty purposes because the Secretary cannot have taken into account the requisite factors in determining value for royalty purposes on the basis of those Statements of Account alone. I adhere to my conclusion that whatever factors go into the formulation of those Statements of Account, the Statements reflect sales price received by the lessees for the quantities of oil and gas reported therein. Sales price may be taken by the Secretary to be conclusive evidence of value for royalty purposes. Standard Form 157, paragraph 3(c); 30 CFR 221.47 (1977). His action in doing so does not constitute an abuse of its discretion.

Plaintiff's claim that it has no means by which to timely appeal the Secretary's monthly determination of value is raised for the first time in the Motion to Revise. It is true that the procedure in actual practice by which the Bureau of Indian Affairs receives no copy of the monthly Statements of Account until ninety days after payment is made by defendants appears to be in conflict with the requirement that notice of appeal be given within thirty days of the action complained of. *See* 30 CFR 290 (1977). While the Secretary's month by month determination of value for royalty purposes may not for all practical purposes be appealable, the procedure itself is subject to appeal. If the Secretary's procedure does

not afford plaintiff an opportunity to make timely appeal under the regulations, plaintiff may seek one of two alternatives. It may institute an action to require that the billing procedure in practice be altered to afford plaintiff its due process right to pursue administrative appeal of the month by month determinations of value or it may seek to require that the regulation setting out the requirements for appeal of administrative action, i.e., 30 CFR 290 (1977), be conformed to actual practice to permit plaintiff sufficient time in which to timely prosecute appeals from the monthly Statements of Account. Neither of these alternatives conflict with my finding that the Secretary has made a determination of value for royalty purposes.

While it is regrettable that the Secretary's action, or more accurately his inaction, in doing no more than accepting the lessees' monthly Statements of Account and basing his determination of value for royalty purposes thereon, may not be in the best interests of plaintiff and further may not result in most profitable royalties due plaintiff from its leases, such action falls within the range of discretion allowed the Secretary. Unfortunately, whether or not I am in agreement with the Secretary's course of action or whether I think the Secretary ought to have done, or ought to be doing, more on behalf of plaintiff is not the point. It is not within my province, having found the Secretary to have acted within his discretion, to order him to do otherwise. Plaintiff's motion to revise will be denied.

Plaintiff has moved for leave to file its Second Amended Complaint. Rule 15(a) of the Federal Rules of Civil Procedure dictates that leave to amend "shall be freely given when justice so requires." Leave to amend shall be granted absent good reason to the contrary. *Foman v. Davis*, 371 U.S. 178, 182 (1962). Whether or not to permit a party to amend its pleadings is left to the sound discretion of the trial court. *Id.* Undue delay and preju-

dice to the opposing party are the primary factors to be considered regarding leave to amend. *R.E.B., Inc. v. Ralston Purina Co.*, 525 F.2d 749, 751 (10th Cir. 1975). Only prejudice amounting to "grave injustice" justifies refusal to permit amendment. *Patton v. Guyer*, 443 F.2d 79, 86 (10th Cir. 1971). Having considered the motion and memorandum briefs of counsel and being fully advised in the premises, I find that plaintiff's Second Amended Complaint raises no substantially new legal issues, that it raises claims arising out of the same nucleus of facts and transactions described in plaintiff's original Complaint and therefore relates back to the date of that Complaint, that the issues raised in the Second Amended Complaint will not result in an unreasonable amount of additional discovery or a substantial delay in this action's progress toward trial, that plaintiff has not sought to amend after undue delay and that permitting plaintiff to so amend will not cause defendants prejudice amounting to grave injustice. Now, Therefore,

IT IS ORDERED that plaintiff be, and hereby is, granted leave to file its Second Amended Complaint. The Clerk of the Court shall file plaintiff's Second Amended Complaint this date. Defendants shall file their answers to the Second Amended Complaint within ten (10) days.

IT IS FURTHER ORDERED that plaintiff's motion to revise the Memorandum Opinion and Order of this Court filed September 7, 1978, be, and hereby is, denied.

IT IS FURTHER ORDERED that this action be, and hereby is, set for trial on the merits on April 2, 1979, at 9:00 A.M.

/s/ E. L. Mechem
United States District Judge

APPENDIX E

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF NEW MEXICO

No. 75-247-M Civil

THE JICARILLA APACHE TRIBE,
Plaintiff,

vs.

SUPRON ENERGY CORPORATION, SOUTHLAND ROYALTY CORPORATION, EXXON CORPORATION, and CECIL B. ANDRUS, Secretary of Interior of United States of America,
Defendants.

[Filed Apr. 13, 1979]

MEMORANDUM OPINION

Plaintiff, the Jicarilla Apache Tribe (Tribe), filed its Second Amended Complaint on December 19, 1978, alleging in two separate Causes of Action that defendants, Supron Energy Corporation (Supron), formerly Southern Union Production Company, Southland Royalty Corporation (Southland), successor to Aztec Oil and Gas Company, and Exxon Corporation (Exxon), all foreign corporations, breached various oil and gas leases pertaining to Tribal lands entered into by defendants, or their precedessors in interest, with the Secretary of Interior (Secretary) on behalf of the Tribe. The Secretary, Cecil B. Andrus, is also a named defendant in this action.

Plaintiff further alleges in its Second Amended Complaint that the defendant energy companies have engaged in concerted illegal activities between and among themselves in violation of the federal antitrust laws. Specifically, it is alleged in the First Cause of Action that Supron, Southern Union Gas Company (now Gas Company of New Mexico (GCNM)) and Southern Union Gathering Company [1], respectively, conspired to fix prices and conceal the actual consideration received for gas from Tribal leaseholds. The Tribe alleges that royalties accounted for to the United States Geological Survey (USGS) were paid to the Tribe on the basis of prices set below market value for gas drawn from the Tribe's lands and sold by defendants Supron and Southland to GCNM. Plaintiff claims that the alleged conspiracies are continuing in nature and are in violation of Section 1 of the Sherman Antitrust Act, 15 U.S.C. § 1 (1976). Plaintiff seeks treble damages based on defendants' concerted activities pursuant to § 4 of the Clayton Antitrust Act, 15 U.S.C. § 15 (1976).

Plaintiff alleges in the Second Cause of Action that Supron and Southland, and Supron and Exxon, respectively, conspired to conceal from the USGS and the Tribe the potential for development of leases held by defendants on Tribal lands in order to hold the leases without production for speculative purposes, in restraint of trade and in violation of Section 1 of the Sherman Antitrust Act, 15 U.S.C. § 1. As with its claim in the First Cause

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[1] Both GCNM and Southern Union Gathering Company were originally named defendants in this action. Defendants' Stipulation for Settlement, agreed to by plaintiff and these two defendants on October 21, 1976, was filed in this action (Docket #112). A Partial Final Judgment and Decree based on the Stipulation for Settlement (and on a Supplemental Stipulation for Settlement not relevant hereto) and filed November 10, 1976, terminated these defendants' participation in the case. The terms of the Stipulation nevertheless continue to affect the parties and issues remaining. *See, infra* at p. 10.

of Action, plaintiff alleges the continuing nature of the conspiracies herein alleged. Plaintiff seeks treble damages on the alleged antitrust violations and further seeks declaratory judgment based on the alleged breach of contract insofar as it claims defendants have failed to diligently develop their leases and drill offset wells as required by the leases. Such a declaration would subject the leases by their own terms to cancellation by the Secretary.

In response to plaintiff's Second Amended Complaint, Southland answered as to the First Cause of Action, raising several affirmative defenses, and filed a motion to dismiss the Second Cause of Action for failure to state a claim, pursuant to Rule 12(b)(6), F.R.C.P. Southland later filed a motion to dismiss the Second Amended Complaint for lack of subject matter jurisdiction, pursuant to Rule 12(b)(1), or, in the alternative, for summary judgment, pursuant to Rule 56. Supron filed its Answer to the Second Amended Complaint and having set out its affirmative defenses, requested that they be treated as motions under Rule 12(b), pursuant to Local 5(c), Rules of the United States District Court for the District of New Mexico. Exxon answered as to the First Cause of Action, listing its affirmative defenses thereto, and in a Second Amended Motion to Dismiss plaintiff's Second Cause of Action for failure to state a claim, seeks dismissal of the Second Cause of Action, or, in the alternative, dismissal of the antitrust claim against it in the Second Cause of Action. Plaintiff filed a consolidated response to defendants' motions and oral argument on the motions was held on March 16, 1979.

Subject Matter Jurisdiction

Defendants' various motions are directed primarily at plaintiff's antitrust claims. Defendants all asserted that lack of subject matter jurisdiction bars cognizance of the antitrust claims set out in both Causes of Action in

plaintiff's Second Amended Complaint. Unlike a motion to dismiss for failure to state a claim on which relief can be granted, on a motion to dismiss for lack of subject matter jurisdiction, plaintiff's allegations of fact are not necessarily taken to be presumptively true. The Court may evaluate for itself the merits of plaintiff's jurisdictional claims and the plaintiff has the burden of proving that jurisdiction does exist. *Mortensen v. First Federal Savings and Loan Ass'n*, 549 F.2d 884, 891 (3rd Cir. 1977). The difficulty in resolving questions as this in antitrust cases arises from the language of Section 1 of the Sherman Act which binds together the jurisdictional basis for the action and a necessary element of the claim itself. This procedural problem has resulted in varying conclusions among the Circuits. *See*, cases collected in *Mortensen*, 549 F.2d at 892-94. *See also, George C. Frey Ready-Mix Concrete, Inc. v. Pine Hill Concrete Mix Corp.*, 554 F.2d 551, 554 n.3 (2nd Cir. 1977).

The Supreme Court, in *Hospital Building Co. v. Trustees of Rex Hospital*, 425 U.S. 738 (1976), considered this problem and concluded that whether viewed under Rule 12(b)(1) or 12(b)(6), the analysis is not different:

> In either event, the initial inquiry is into the adequacy of the nexus between respondents' conduct and interstate commerce that is alleged in the complaint.

Id., at 742n.1. *But see, George C. Frey Ready-Mixed Concrete, Inc. v. Pine Hill Concrete Mix Corp.*, 551 F.2d at 554n.3 ("A motion to dismiss for lack of jurisdiction . . ., is inappropriate in antitrust] cases unless the interstate commerce claim is patently frivolous. [citations omitted]."). The Court in the *Rex* case also noted that as to Congress' power under the Commerce Clause, "[s]ubsequent decisions by this Court have permitted the reach of the Sherman Act to expand along with expanding notions of congressional power. [citations omitted)." *Id.*, at 743n.2; *Gulf Oil Corp. v. Copp Paving Co., Inc.*, 419

U.S. 186, 194-95 (1974). And the fear of preventing plaintiffs from litigating viable antitrust claims because of a questionable jurisdictional foundation has resulted in the conclusion that less is required to withstand a pretrial jurisdictional attack in antitrust cases. *Canadian American Oil Co. v. Union Oil Co. of California*, 577 F.2d 468, 471 (9th Cir. 1978); *Mortensen, supra.*

Absent a finding that there exists some nexus between defendants' concerted activities and interstate commerce, subject matter jurisdiction over a federal antitrust claim cannot exist. Defendants contend that because the gas drawn from the Tribe's lands is sold, processed, transported and consumed solely in intrastate commerce, within the borders of the State of New Mexico, plaintiff cannot maintain its federal antitrust claims. Plaintiff, however, has produced evidence by affidavit that liquid byproducts extracted from gas from its lands is transported in interstate commerce. Southland insists this fact if true, is irrelevant as to itself since it sells gas it draws from the Tribe's lands at the wellhead, in New Mexico, and any entry of that gas into interstate commerce further down the line may not be imputed to it to establish the nexus required under the federal antitrust laws. Southland's argument is misconceived insofar as it ignores its own status as an alleged coconspirator. The entire scope of the alleged conspiracy may be considered in determining whether the requisite nexus exists, and, if found, it is sufficient to permit the Tribe to maintain its antitrust claims against all co-conspirators. In any event, the teaching of the *Rex* case permits a look beyond whether the gas produced from the Tribe's lands crosses state lines. *Hospital Building Co. v. Trustees of Rex Hospital*, 425 U.S. at 744-76.

On the basis of the case law and the facts presented, I conclude plaintiff has sustained its burden to withstand notions of congressional power. [citations omitted]." *Id.*, at 743n.2; *Gulf Oil Corp. v. Copp Paving Co., Inc.*, 419

the oil and gas business, of which their New Mexico activities, including their development of plaintiff's leases, are a part, and interstate commerce to sustain a finding that defendants' activities, if not necessarily "in" interstate commerce, "affect" interstate commerce. *Rex*, 425 U.S. at 744. "The effect on interstate commerce need not [be] gargantuan nor precisely mathematicized. It is sufficient if it is more than merely inconsequential. [citations omitted]." *Woods Exploration & Producing Co., Inc. v. Aluminum Company of America*, 438 F.2d 1286, 1303 (5th Cir. 1971).

The requirement of the *Rex* case, that there be an "'unreasonable burden on the free and uninterrupted flow'" of interstate commerce, *Rex*, 425 U.S. at 746, is met here by the fact that defendants are large interstate corporations whose business of gathering, producing and selling, natural gas taken from the Tribe's lands must necessarily have been an integral part of their larger, clearly interstate, business operation. As the Supreme Court noted in the *Rex* case, defendants in seeking to dismiss plaintiff's antitrust claim on the basis of jurisdiction face a "concededly rigorous standard." *Id.*, at 746. And, again, as the Court noted, whether plaintiff can make a *prima facie* case on its antitrust claims is another question. *Id.*, at 747n.5.

Subject matter jurisdiction is a question of law which may be raised at any time by the parties or the Court. Therefore, my decision that plaintiff's action withstands defendants' pre-trial jurisdictional attacks does not settle the question conclusively. The standard by which I have decided defendants' 12(b)(1) claims is not the same as the one to be applied on the merits of plaintiff's antitrust claims, an element of which, as discussed above, is the nexus between defendants' activities and interstate commerce. *Canadian American Oil Co. v. Union Oil Co. of California, supra.* Should it appear at trial, or thereafter, that subject matter jurisdiction over plaintiff's anti-

trust claims may not in fact exist, the question will be taken up at that time.

Defendants also claim that subject matter jurisdiction over plaintiff's Second Cause of Action is lacking because the claims therein are based in contract, are not based on a federal question and therefore form no basis for the assertion of federal jursdiction. I have determined that plaintiff's antitrust claims state a claim sufficient to withstand defendants' pre-trial attacks, clearly forming a basis for federal jurisdiction when coupled with the language of 28 U.S.C. 1362 (1976). Aside from this, however, the Tribe's contract claims, based on its leases with defendants, themselves suffice to establish federal jurisdiction over the Second Cause of Action.

The Tribe's leases, entered into on its behalf by the Secretary, are subject to the continuing supervision of the Secretary. *Poafpybitty v. Skelly Oil Co.*, 390 U.S. 365, 372-73 (1968). Given the fiduciary obligation of the Secretary to protect the Tribe's proprietary interests, such as their interests in the leases held by defendants, the nature of the Tribe's contract claims is decidedly federal. *Oneida Indian Nation of New York v. County of Oneida, New York*, 414 U.S. 661 (1974). This supports my conclusion that the Tribe's contract claims are independently founded in federal law and that jurisdiction is proper under 28 U.S.C. § 1362.

Standing

The second defect attributed to plaintiff's antitrust claims by all defendants is its asserted lack of standing to sue under the federal antitrust laws. Standing to sue under § 4 of the Clayton Antitrust Act, 15 U.S.C. § 15, is a question of law to be determined by the trial court. *John Lenore & Co. v. Olympia Brewing Co.*, 550 F.2d 495, 498 (9th Cir. 1977). Three tests for standing have been adopted by the federal Circuit Courts of Appeals. The "direct injury" test requires just that, a direct in-

jury to plaintiff resulting from defendants' acts alleged to have been in violation of the antitrust laws. *Loeb v. Eastman Kodak Co.*, 183 Fed. 704 (3rd Cir. 1910). Under this test, incidental, consequential or derivative injury to plaintiff is judged to be "too remote" to confer standing to sue under the antitrust laws. *Nationwide Auto Appraiser Service, Inc. v. Ass'n of Casualty and Surety Cos.*, 382 F.2d 925, 929 (10th Cir. 1967). It is well to note that the questions of who has sustained antitrust injury and whose injury is too remote to confer standing to sue under the antitrust laws are distinct from one another. *Illinois Brick Co. v. Illinois*, 431 U.S. 720, 728n.7 (1977).

The "target area" test requires that

> [t]here . . . be an identification of the affected area of the economy which is the target of the alleged anticompetitive conduct. And, it must be determined that the alleged injury was in that area. [citations omitted].

John Lenore & Co. v. Olympia Brewing Co., 550 F.2d at 499; *Conference of Studio Unions v. Loew's, Inc.*, 193 F.2d 51 (9th Cir. 1951), cert. den., 342 U.S. 919 (1952). Under the target area test, it is not enough for plaintiff to show it was "hit" by defendants' concerted activities; it must show it was "aimed at." *Karseal Corp. v. Richfield Oil Corp.*, 221 F.2d 358, 362 (9th Cir. 1955).

The third test for standing, recently adopted by the United States Court of Appeals for the Third Circuit, is essentially the standing test developed by the United States Supreme Court in *Ass'n of Data Processing Service Organizations, Inc. c. Camp*, 397 U.S. 150 (1970). *Malamud v. Sinclair Oil Corp.*, 521 F.2d 1142 (6th Cir. 1975). In a reasoned opinion, the Third Circuit concluded that the two-pronged approach of *Data Processing*, looking to see if plaintiff has alleged " 'injury in fact,' " and if " 'the interest sought to be protected . . . [was] arguably

within the zone of interests to be protected,' " *Malamud v. Sinclair Oil Corp.*, 521 F.2d at 1145, quoting from *Data Processing*, 397 U.S. at 152-53, sufficiently satisfied Congress' intent that the antitrust laws be limited in their application to plaintiffs who have suffered an "*anti-trust* injury . . . of the type the antitrust laws were intended to prevent and that flows from that which makes defendants' acts unlawful." *Brunswick Corp. v. Pueblo Bowl-O-Mat*, 429 U.S. 477, 489 (1977) (emphasis in original).

Plaintiff argues that the "direct injury" test ought to be applied in this case, citing the Tenth Circuit's decision in *Nationwide Auto Appraisers Service, Inc. v. Ass'n of Casualty and Surety Cos., supra.* Defendants claim the "target area" test to be the better rule and the majority rule, and assert further that its application in this case is not foreclosed by the *Nationwide* case. Neither side has claimed knowledge of or reliance on the *Data Processing* test set out in *Malamud v. Sinclair Oil Corp., supra.* I need not decide which test to use to determine whether plaintiff has standing to prosecute its antitrust claims, as I have concluded that plaintiff has made the requested showing of standing to sue under any of these tests.

Under the terms of its leases, plaintiff may give timely notice to its lessees and take its royalties in kind. Plaintiff alleges in its Second Amended Complaint that it desires to take royalties in kind but that the Stipulation for Settlement Agreement it effected with GCNM and Southern Union Gathering Company, *see, supra* at p. 2n.1, prevents it from doing so. As set out in the Stipulation, it appears that other parties, including Supron, have exclusive contractual rights to process gas and liquid by-products derived from plaintiff's leases. The Tribe's decision to take royalties in kind might impair those parties' contractual rights. The Stipulation states that GCNM is excused from gathering or processing the

Tribe's royalty gas taken in kind until the contractual rights and obligations referred to are settled by agreement of the parties, which has not occurred, or by a court of competent jurisdiction. Stipulation for Settlement, ¶¶ 2, 3.

I understand this language in the Stipulation to mean that it is the Tribe's desire to become a competitor in the business of the sale of natural gas, necessarily then, a competitor with defendant energy companies. As a potential competitor, plaintiff falls within the target area of defendants' alleged concerted activities and has allegedly sustained direct injury by reason thereof. *Solinger v. A & M. Records, Inc.*, 586 F.2d 1304, 1309-10 (9th Cir. 1978), petition for cert. filed, 47 U.S.L.W. 3587 (U.S. Mar. 6, 1979) (Nos. 78-1315, 78-1317). Defendants resist such an interpretation of the standing doctrine by asserting that plaintiff is not a competitor and therefore cannot have standing to sue under the federal antitrust laws. "The antitrust laws, however, were enacted for 'the protection of *competition*, not *competitors*,' [citation omitted]." *Brunswick Corp. v. Pueblo Bowl-O-Mat*, 429 U.S. at 488 (emphasis in original).

Plaintiff's claim that defendants' activities have resulted in lesser royalties as a result of both the alleged price fixing and restraint of trade constitutes direct and tangible injury. Defendants insist that plaintiff, as a non-operating owner/lessor, has no standing to sue its lessees for antitrust violations. Defendants rely primarily on the theatre cases for their contention. *Calderone Enterprises Corp. v. United Artists Theatre Circuit, Inc.*, 454 F.2d 1292 (2d Cir. 1971), cert. den., 406 U.S. 930 (1972); *Melrose Realty Co. v. Loew's, Inc.*, 234 F.2d 518 (3rd Cir.), cert. den., 352 U.S. 890 (1956), reh. den., 355 U.S. 900 (1957); *Harrison v. Paramount Pictures, Inc.*, 115 F.Supp. 312 (E.D.Pa. 1953). In these cases, as defendants correctly point out, the lessor was denied

standing to sue his lessee because the conspiracy alleged was not directed at the lessor; the lessor's injury was *incidental* to the conspiracy. As such, the cases are inapposite.

Here the Tribe alleges that the price fixing conspiracy was directly aimed at the Tribe by causing lesser royalties to accrue on defendants' leases than were actually due. The result of the alleged conspiracy to limit development was not materially different. And in each case, defendants point nowhere else in an attempt to establish an aim of the conspiracies other than to injure the Tribe. Plaintiff is the victim clearly intended to be harmed by these alleged activities and has made a claim of antitrust injury of the type of antitrust laws were intended to remedy. *Brunswick Corp. v. Pueblo Bowl-O-Mat, supra; Cromar Co. v. Nuclear Materials and Equipment Corp.*, 543 F.2d 501, 506 (3rd Cir. 1976).

Defendants' claim that the gas remains in the ground notwithstanding the alleged lack of development, that given the rising nature of natural gas prices future processing of that gas can only result in higher royalties to the Tribe, and that therefore the Tribe has sustained no injury on which to predicate standing, is not persuasive. Drainage may prevent recovery in the future of as large a volume of gas as might have been withdrawn under a regime of orderly, timely development of the leases. No answer to such speculation one way or the other has been offered by the parties.

While plaintiff's substantive claims are subject to the conventional burden of proof at a hearing on the merits, they support a finding of standing to sue in the face of defendants' motions. Accordingly, defendants' motions to dismiss or for summary judgment predicated on plaintiff's lack of standing to sue under the antitrust laws will be denied. Defendants' affirmative defenses raising this same claim will be stricken.

Immunity

Defendants claim their alleged concerted activities are immune from scrutiny under the federal antitrust laws. It is their contention that because the Secretary has extensive authority to regulate in the area of Indian oil and gas leases, *see, Poalpybitty v. Skelly Oil Co.*, 390 U.S. at 372-73, application of the antitrust laws in this case would impermissibly infringe on the Secretary's "adjudicative and remedial jurisdiction" in this area. *Ricci v. Chicago Mercantile Exchange*, 409 U.S. 289, 299 (1973). The question of immunity arises when

> conduct seemingly within the reach of the antitrust laws is also at least arguably protected or prohibited by another regulatory statute enacted by Congress.

Id., at 299-300. Congress may grant, and has granted, express exemptions from the antitrust laws. The antitrust laws do not apply to labor organizations, 15 U.S.C. § 17 (1976), or to acts done which are authorized by numerous federal administrative agencies, including the Civil Aeronautics Board, the Federal Communications Commission, the Interstate Commerce Commission, the Federal Power Commission, the Securities and Exchange Commission in certain defined areas, the United States Maritime Commission and the Secretary of Agriculture, 15 U.S.C. § 18 1976). *See also, United States v. Philadelphia National Bank*, 374 U.S. 321, 350 n.27 (1963); 49 U.S.C. § 5(12) (1976).

Implied exemptions have been recognized only sparingly by the United State Supreme Court. *See United States v. National Ass'n of Securities Dealers*, 422 U.S. 694, 719-20 (1975); *Ricci v. Chicago Mercantile Exchange*, 409 U.S. at 299-300 n.12; *Silver v. N. Y. Stock Exchange*, 373 U.S. 341 (1963); *Pan American World Airways, Inc., v. United States*, 371 U.S. 296 (1963). "[T]he antitrust laws must give way if the regulatory scheme established by the [regulatory statute] is to work.

[citation omitted]." *United States v. National Ass'n of Securities Dealers*, 422 U.S. at 729-30. "Repeals of the antitrust laws by implication from a regulatory statute are strongly disfavored, and have only been found in cases of plain repugnancy between the antitrust and regulatory provisions [footnotes omitted]." *United States v. Philadelphia National Bank*, 374 U.S. at 350-51.

Defendants have cited no statutory regulatory power of the Secretary which conflicts with the "felt indispensable role of antitrust policy in the maintenance of a free economy," *United States v. Philadelphia National Bank*, 374 U.S. at 348, nor have they established, beyond general conclusory statements in their briefs, that any such regulatory scheme of the Secretary's, assuming one exists, cannot work because it is inhibited by the reach of the antitrust laws. Were immunity to be found extant in this case, the proper resolution would be not to dismiss plaintiff's antitrust claims, but rather to stay proceedings pending determination by the Secretary of issues subject to his regulation, which, of course, would be subject to judicial review in this Court. And, it is clear that "agency approval of particular transactions does not itself confer antitrust immunity." *United States v. National Ass'n of Securities Dealers*, 422 U.S. at 739 (White, J., diss.).

The immunity defense is often raised in conjunction with claims that actions in the district court be stayed or dismissed because primary jurisdiction lies in an administrative agency or because plaintiff has failed to exhaust administrative remedies. *Cf., Ricci v. Chicago Mercantile Exchange, supra.* In *Ricci*, Mr. Justice Douglas dissented, illuminating a point which I adopt in denying defendants' motions based on these defenses.

> [I]t would appear to be an anomaly to direct the plaintiff in a civil action to a federal supervising agency for a determination as to whether the regulations which it is charged to enforce have been vio-

> lated, when the agency has, by its inaction, already shown every indication of sanctioning the alleged violation. By remanding, we are requiring the petitioner to seek from the regulators an admission of their failure to regulate (or negligence in regulating).
>
> The odds of petitioner's getting the [federal agency] now to find a violation in contradiction of its past inaction do not, in my view, justify the expense and delay to the petitioner. In the interests of orderly and efficient judicial administration, parties are not generally required to engage in futile gestures.

Id. 409 U.S. at 308-09 (Douglas, J., diss.). The memorandum of the Secretary filed with the Court March 12, 1979 adds emphasis, although little is necessary, to Mr. Justice Douglas' plea in dissent. The memorandum reinforces my conclusion that the Secretary, although imbued with power to act, either will not or cannot do what is asked of him.

The Secretary, in his memorandum, states that his agency, acting through the USGS, lacks the manpower to make the determinations sought by plaintiff and ordered by this Court. This excuse for nonaction, although it may be correct, is not justification for failing to do those acts required of him in his supervisory capacity as fiduciary of the federal trust responsibility to Indian tribes regarding the Tribe's leases. Since it appears that remand to the Secretary would serve no useful purpose, I decline to rely further on the Secretary's expertise or his power to act in this area. Accordingly, I will deny defendants' motions insofar as they are based on the doctrines of immunity, primary jurisdiction and exhaustion of administrative remedies.

Laches, Statutes of Limitations

Defendant energy companies have raised as affirmative defenses the claims that plaintiff's action is barred by

laches, that its contract action is barred by the New Mexico statutes of limitations relating to contract actions, N.M.S.A. § 37-1-3 (1978 Comp.), and that its antitrust claims are barred by 15 U.S.C. § 15b. Laches is not applicable to an antitrust claim seeking damages under § 4 of the Clayton Act because of the overriding application of § 15b. *Cf., International Tel. and Tel. Corp. v. General Tel. & Electronics Corp.*, 518 F.2d 913, 928 (9th Cir. 1975). "Lapse of time alone does not constitute laches [footnote omitted]." *Shell v. Strong*, 151 F.2d 909, 911 (10th Cir. 1945). Laches applies when, because of the delay in asserting one's rights, prejudice or injustice would inure to the defendant by enforcing plaintiff's rights.

I find, as a matter of law, that no prejudice or injustice will fall on defendants should plaintiff prevail on its contract claims. Plaintiff seeks damages from 1970 to date. Its attempts to remedy what it understood to be violations of its leases with defendants began in 1973 when it sought the assistance of the Secretary. This lawsuit was filed in 1975. The time involved has not been so great that prejudice or injustice to defendants will have occurred on account of the claimed delay should plaintiff prevail on the merits. Defendants have not suggested, nor can I imagine, any basis for prejudice or injustice justifying application of the laches doctrine other than the claimed delay in filing this suit.

Were this a diversity action, a New Mexico statute of limitations relating to the contract claim would apply. *Erie Railroad Co. v. Thompkins*, 304 U.S. 64 (1938). But this is not a diversity action, and although Congress has in the past specifically directed the application of state statutes of limitations to federal cases, *see, e.g.*, 25 U.S.C. § 347 (1976) (state statutes of limitations applicable to suits involving patent lands), no such Congressional action is relevant to this case. Defendants' affirmative defenses based on the New Mexico statute of

limitations, N.M.S.A. § 37-1-3 (1978 Comp.), will be stricken.

It does not appear that there exists a relevant federal statute of limitations insofar as the time for commencing an action on behalf of the Indians is concerned. The Indians may commence actions on their own behalf, notwithstanding the fact that the United States Government, and more particularly, the Secretary of the Interior, is entrusted with a fiduciary responsibility to protect the rights of the several Indian tribes. *State of New Mexico v. Aamodt*, 537 F.2d 1102, 1107 (10th Cir. 1976); 25 U.S.C. § 2 (1976). The Secretary's presence in this action as a party defendant evidences one aspect of the reasoning behind permitting the Indians to prosecute their own actions. *Poafpybitty v. Skelly Oil Co.*, 390 U.S. at 374. Were the Government to have initiated this action on behalf of the Tribe, however, the time for commencing it would have been dictated by 28 U.S.C. § 2415 (a) (1976), which requires that actions for money damages brought by the United States commence within six years and ninety days of the time the right of action accrues. Even if, by analogy, this statute were applied to this case, the Tribe, seeking damages from 1970 to date, filed this action in 1975, within the required time.

Defendants claim 15 U.S.C. § 15b (1976) bars plaintiff's antitrust claims. Section 15b requires that an action be brought within four years of when it accrues. An antitrust action accrues when the defendant commits an act which injures a plaintiff's business, *Zenith Radio Corp. v. Hazeltine Research, Inc.*, 401 U.S. 321, 338, reh. den., 401 U.S. 1015 (1971).

A defendant's active, fraudulent concealment of antitrust violations causing plaintiff injury tolls the running of the time period under § 15b. *Public Service Company of New Mexico v. General Electric Co.*, 315 F.2d 306, 310 (10th Cir.), cert. den. 374 U.S. 809 (1963). To toll the statute, fraudulent concealment must be accompanied by

a showing that the plaintiff's exercise of due diligence did not uncover the injury caused to plaintiff. *Bailey v. Glover*, 88 U.S. (21 Wall.) 342, 348 (1874). As fraud is a fact question, I will reserve ruling on when the time period set out in § 15b began to run with regard to plaintiff's antitrust claims subject to the showing required by the case law. Accordingly, defendants' motions to dismiss on the basis of 15 U.S.C. § 15b, or more accurately, their attempt to limit the scope of plaintiff's antitrust claims to the four years immediately preceding the time this action was commenced, will be denied. Defendants' affirmative defenses based on § 15b, however, will not be dismissed.

Plaintiff's Release of GCNM and Southern Union Gathering Co.

Defendant Supron has raised as an affirmative defense to plaintiff's First Cause of Action the claim that plaintiff's release of GCNM and Southern Union Gathering Company as parties defendant to this action acts to estop plaintiff's claim of conspiracy between and among Supron and the released defendants. This release has left Supron as the only named conspirator in the First Cause of Action. Hornbook law requires the concerted activity of two or more entitites to constitute a violation of the antitrust laws. There being only one conspirator named in the First Cause of Action, the others having been released by plaintiff, Supron contends that plaintiff's claim fails to state a claim on which relief can be granted, and that therefore, Supron's motion to dismiss plaintiff's First Cause of Action should be granted.

"An antitrust action is in the nature of a tort action and defendants are jointly and severally liable" if liability is found. *Solomon v. Houston Corrugated Box Co., Inc.*, 526 F.2d 389, 392n.4 (5th Cir. 1976). "Thus an antitrust plaintiff may choose to sue but one of several co-conspirators, *Walker Distributing Co. v. Lucky Lager*

Brewing Co., 323 F.2d 1, 8 (9th Cir. 1963), and that one co-conspirator will be responsible for the entire amount of damages caused by all. (citation omitted)." *Wainwright v. Kraftco Corp.*, 58 F.R.D. 9, 12 (N.D.Ga. 1973). Or, as in this case, an antitrust plaintiff may choose to sue a number of co-conspirators, effect binding releases with one or more of them and continue to pursue his antitrust action against the one defendant remaining in the suit.

Whether a plaintiff's release with co-conspirators serves to block prosecution of an additional co-conspirator not a party to the release must be determined solely from the intent of the plaintiff. "The straightforward rule is that a party releases only those other parties whom he intends to release." *Zenith Radio Corp. v. Hazeltine Research, Inc.*, 401 U.S. at 347. The Court in the *Zenith Radio* case adopted this rule for antitrust cases after considering the reasons for its initial application in *Aro Mfg. Co. v. Convertible Top Co.*, 377 U.S. 476 (1964), a patent infringement case. *Id.*, at 346. To conclude otherwise, the Court said, "would frustrate partial settlements, and thereby promote litigation, while adoption of the First Restatement rule [requiring express reservation of rights in order to save them] would create a trap for unwary plaintiffs' attorneys." *Zenith Radio Corp. v. Hazeltine Research, Inc.*, 401 U.S. at 347.

By its release of GCNM and Southern Union Gathering Company, the Tribe intended to extinguish its claim against those two parties only. The language of the Stipulation for Settlement could not be more clear:

> GCNM shall pay the Tribe within ten (10) days after the approval of this Stipulation by the Court and entry of the same as its Judgment, the sum of Six Hundred Thousand Dollars ($600,000.00) *for settlement of all claims made by the Tribe against GCNM and Southern Union Gathering Company* in

> this case . . . and for agreement that *all claims and causes of action of the Tribe against GCNM and Southern Union Gathering Company* set forth and alleged in the First Amended Complaint on file herein are released and discharged and *all such claims and causes of action are dismissed with prejudice as to the defendants GCNM and Southern Union Gathering Company.*

Stipulation for Settlement, ¶ 5. (emphasis supplied).

> This Stipulation shall be construed to pertain to *all claims of the Tribe against GCNM and Southern Union Gathering Company* relating to oil and gas . . ., accruing to the date of this Stipulation.

Stipulation for Settlement, ¶ 7. (emphasis supplied).

> All matters in controversy in this case *between the Tribe and the Defendants GCNM and Southern Union Gathering Company* having been settled, the parties hereto request the Court to enter this Stipulation as its Final Judgment in this case, and *the case shall be dismissed with prejudice in its entirety as to GCNM and Southern Union Gathering Company* . . . .

Stipulation for Settlement, ¶ 8. (emphasis supplied).

Plaintiff's intention was to release only the two defendants named in the Stipulation for Settlement. And notwithstanding the conclusion in *Zenith Radio* that express reservation of a plaintiff's rights as against remaining defendants is not required, the Partial Final Judgment and Decree entered on November 10, 1976 evidences that the Tribe did just that in this case:

> IT IS FURTHER ORDERED, ADJUDGED AND DECREED that this action . . . and all claims for relief and causes of action contained therein, hereby are dismissed with prejudice as to Defendants GCNM and Southern Union Gathering Company;

> *provided that all claims* set forth in Plaintiff's First Amended Complaint *and matters in controversy between Plaintiff and the Defendants Southern Union Production Company* [*Supron*], *Aztec Oil and Gas Company* [*Southland*], *Exxon Corporation* and the Secretary of the Interior *shall continue and this settlement shall not be construed as a settlement or determination of any of the issues in this cause except between the parties to said settlement.*

Partial Final Judgment and Decree, ¶ 4. (emphasis supplied).

Plaintiff's release does not prevent it from assembling the proof necessary at a hearing on the merits to establish that Supron and the released defendants conspired in violation of the antitrust laws. The release does not prevent the Tribe from obtaining evidence from the released defendants to be used against Supron in establishing antitrust violations. Indeed, it is likely that the evidence will be more readily forthcoming now that GCNM and Southern Union Gathering are insulated from further liability no matter what their testimony establishes. Defendant Supron's claim of estoppel and its corollary motion to dismiss on the basis of plaintiff's release have no basis in law. The affirmative defenses will be stricken and the motion to dismiss will be denied.

Corporate Identities

Supron raises an additional affirmative defense claiming that the lack of separate corporate identities among the co-conspirators named in plaintiff's Second Amended Complaint bars the prosecution of antitrust claims since a single entity cannot conspire with itself. This argument deserves, and will receive, short shrift. "The fact that there is common ownership or control of the contracting corporations does not liberate them from the impact of the antitrust laws. (citations omitted)." *Tim-*

ken Roller Bearing Co. v. United States, 341 U.S. 593, 598 (1951). "The corporate interrelationships of the conspirators . . ., are not determinative of the applicability of the Sherman Act. That statute is aimed at substance rather than form. (citation omitted)." *United States v. Yellow Cab Co.*, 332 U.S. 218, 227 (1947). *Accord, Perma Life Mufflers, Inc. v. Int'l Parts Corp.*, 392 U.S. 134, 141-42 (1968). Supron's Fourteenth Affirmative Defense will be stricken as having no basis in law.

Public Harm

Supron's Sixteenth Affirmative Defense raises an equally frivolous claim and will also be stricken. A showing of public harm is not a requisite to maintaining an action under Section 1 of the Sherman Act. *Radiant Burners, Inc. v. Peoples Gas Light & Coke Co.*, 364 U.S. 656 (1961) (per curiam). "[T]o state a claim upon which relief can be granted [under 15 U.S.C. § 1] . . ., allegations adequate to show a violation and, in a private treble damage action, that plaintiff was damaged thereby are all the law requires." *Id.*, at 660.

Damages

Defendants have raised plaintiff's failure to plead recoverable damages as affirmative defenses based on which the Second Amended Complaint should be dismissed. Damages is an essential element of the plaintiff's claim of breach of the leases. *Goodwin v. Standard Oil Company of Louisiana*, 290 Fed. 92 (8th Cir. 1923). A lessor may elect to seek his remedy in a breach of lease case such as this, *Julian Petroleum Corp. v. Courtney Petroleum Corp.*, 22 F.2d 360, 362 (9th Cir. 1927), and it may well be failure of proof, but not the unavailability of the remedy, which defeats his action. *Id.* Proof of damages in a case as this necessarily relies on expert opinion testimony, but such evidence may carry plain-

tiff's burden notwithstanding its ultimate inexactitude, this being a question for the factfinder. *Stanolind Oil & Gas Co. v. Kimmel*, 68 F.2d 520, 522 (10th Cir. 1934); 3 Summers Oil & Gas § 433, at 6-15.

Defendants further rely on this Court's Order of September 8, 1978 granting partial summary judgment in their favor on the issue of value to substantiate their claim that, as a matter of law, plaintiff cannot prove recoverable damages. Plaintiff has alleged as part of its antitrust claims conspiracies to fix prices and defraud the USGS by defendants' concerted failure to accurately report to USGS the actual consideration received for gas drawn from the Tribe's lands. If plaintiffs make their proof on this claim, not withstanding my conclusion that the Secretary acted within his discretion in determining value for the purpose of computing the Tribe's royalties pursuant to the terms of its leases held by defendants, that determination will have been based on erroneous information, rendering the Secretary's determinations of value clearly erroneous. If this chain of events is shown to have occurred, plaintiff may well be in a position to prove damages based on inadequate royalties paid to it. Further, should plaintiff prove its claim of conspiracy, its asserted intent to take royalty gas in kind, and thereby become a competitor in the natural gas market, may provide a source of recoverable damages under the antitrust laws. *Woods Exploration & Producing Co., Inc. v. Aluminum Corp. of America*, 438 F.2d at 1310.

Defendants' motions to dismiss, based on plaintiff's failure to allege recoverable damages, will be denied. Should plaintiff fail in its proof of conspiracy, defendants are free to raise the issues claimed herein on motions for directed verdict. Because I am unable to rule on defendants' claims as a matter of law, their affirmative defenses going to the issues of damages and the effect of the September 8, 1978 Order on plaintiff's claim of damages will not be stricken.

Other Matters

Defendant Supron's Affirmative Defenses numbered 9, 10, 11, 12 and 13 will be dismissed as frivolous and having no basis in law. I need not comment on them further.

At oral argument, counsel for both sides requested that I rule on those issues on which I reserved ruling in the September 8, 1978 Order pending the Secretary's determination. Because I find the Secretary's memorandum addressing those issues to be vague and inconclusive, I conclude that material issues of fact remain unresolved and in issue. As a result, I decline to grant summary judgment on those issues in favor of either plaintiff or defendants. They are properly part of those substantive claims to be addressed at the hearing on the merits in this case and will be ruled on at that time.

An Order will be filed in accordance with this Memorandum Opinion.

/s/ E. L. Mechem
United States District Judge

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF NEW MEXICO

No. 75-247-M Civil

THE JICARILLA APACHE TRIBE,
Plaintiff,

vs.

SUPRON ENERGY CORPORATION, SOUTHLAND ROYALTY CORPORATION, EXXON CORPORATION, and CECIL B. ANDRUS, Secretary of Interior of United States of America,
Defendants.

[Filed Apr. 13, 1979]

ORDER

There having been a Memorandum Opinion filed which contains my findings and conclusions of law, having heard oral argument and considered the memoranda of counsel and further being fully advised in the premises; Now, Therefore,

IT IS ORDERED that the motions of defendant Southland Royalty Company to dismiss the Second Amended Complaint for lack of subject matter jurisdiction or in the alternative for summary judgment and to dismiss the Second Cause of Action contained in the Second Amended Complaint for failure to state a claim on which relief can be granted be, and hereby are, denied.

IT IS FURTHER ORDERED that defendant Exxon Corporation's second amended motion to dismiss the Second Cause of Action contained in the Second Amended

Complaint for failure to state a claim on which relief can be granted or in the alternative to dismiss the antitrust claims alleged against Exxon in the Second Cause of Action be, and hereby is, denied.

IT IS FURTHER ORDERED that Southland's first, second and third affirmative defenses as to the First Cause of Action in the Second Amended Complaint, insofar as the third affirmative defense is based on claims of laches and the application of N.M.S.A.37-1-3 (1978 Comp.), be, and hereby are, stricken.

IT IS FURTHER ORDERED that Exxon's first, second, third, fourth and fifth affirmative defenses to the First Cause of Action in the Second Amended Complaint, insofar as the fifth affirmative defense is based on N.M.S.A.37-1-3 (1978 Comp.), be, and hereby are, stricken.

IT IS FURTHER ORDERED that defendant Supron Energy Corporation's first, second, third, fourth, fifth, sixth, seventh, ninth, tenth, eleventh, twelfth, thirteenth, fourteenth, sixteenth and seventeenth affirmative defenses to the Second Amended Complaint, except insofar as the seventh affirmative defense is based on 15 U.S.C. § 15b, be, and hereby are, stricken.

IT IS FURTHER ORDERED that as to those matters on which ruling in the September 8, 1978 Memorandum Opinion and Order was deferred pending the Secretary's determination, the parties' motions for summary judgment be, and hereby are, denied.

IT IS FURTHER ORDERED that as to those portions of the Second Amended Complaint to which certain of the defendants have not answered in light of pending motions to dismiss which have been denied by this Order, answers shall be filed no later than April 23, 1979.

/s/ E.L. Mechem
United States District Judge

APPENDIX F

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF NEW MEXICO

No. 75-247-M Civil

THE JICARILLA APACHE TRIBE,
Plaintiff,

v.

SUPRON ENERGY CORPORATION, *et al.*,
Defendants.

[Filed November 5, 1979]

MEMORANDUM OPINION

There having been a bench trial on the merits in this action in May and June, 1979, the following shall constitute my Findings of Fact and Conclusions of Law, pursuant to Rule 52 of the Federal Rules of Civil Procedure.

Plaintiff, The Jicarilla Apache Tribe (Tribe), in its Second Amended Complaint seeks treble damages based on alleged antitrust violations as well as damages and an accounting based on alleged breaches of the several leases which are the subject matter of this litigation. Defendants to these claims are Supron Energy Corporation, formerly Southern Union Production Company (Supron), Southland Royalty Company, formerly Aztec Oil and Gas Company (Southland or Aztec), and Exxon Company, U.S.A., formerly Humble Refining Company (Exxon). Not all of plaintiff's several claims are lodged

against each of these defendants-lessees, as is more fully set out below.

Gas Company of New Mexico, formerly Southern Union Gas Company (GCNM or SUG), and Southern Union Gathering Company (SUGC), both wholly owned subsidiaries of Southern Union Company (Southern Union), originally were named defendants to this action. GCNM and SUGC effected a settlement agreement with the Tribe in late 1976. GCNM remains a third-party defendant to this action by virtue of a cross-claim lodged by Southland alleging a claim of indemnity under the gas purchase contract effected between these two companies for excess royalties Southland may be found to owe the Tribe.

Also a named defendant is Cecil Andrus, Secretary of the Interior (Secretary), by virtue of the Tribe's claim that the Secretary has breached his fiduciary obligation to the Tribe arising under provisions of the several leases which are the subject matter of this litigation. As to the defendant Secretary, the Tribe seeks declaratory judgment that the alleged breach of fiduciary duty in fact occurred as well as an accounting for royalties allegedly owing by defendants-lessees which the Secretary and his named representatives have failed to secure for the Tribe under the leases in question.

Plaintiff, at the trial on the merits in this action, moved to conform its pleadings to the evidence, which motion was granted. Accordingly, issues raised at trial which were not set out in plaintiff's Second Amended Complaint will be considered in addition to the issues raised therein. Plaintiff's claims have been at times as the shifting sands. Any issues plaintiff claims to have raised which are not considered in this Opinion are deemed to have fallen of their own weight or lack thereof.

Plaintiff is an Indian Tribe organized and incorporated under the laws of the United States of America, 25 USC

476-7, residing on an Executive Order Reservation in Rio Arriba and Sandoval Counties in Northern New Mexico. Defendants Supron, Southland and Exxon are foreign corporations qualified to do business or doing business in New Mexico who have their principle places of business outside the State of New Mexico. Subject matter jurisdiction is proper pursuant to 28 USC 1331(a) and 1362, 5 USC 701-06 and 15 USC 15.

Defendant Supron, whose name was changed from Southern Union Production Company in April, 1977 by action of its stockholders, was originally an inactive corporation which was a wholly owned subsidiary of Southern Union. Southern Union's ownership of Supron's stock was reduced to approximately 70% in the early 1970's and further reduced to approximately 28% in December of 1976. Defendant Southland acquired Aztec by merger subsequent to the filing of the original complaint in this action in which Aztec was a named defendant. Southland succeeded to this litigation by virtue of the merger. Aztec was originally organized in 1950 as a wholly owned subsidiary corporation of Southern Union and was subsequently spun off in 1954. SUGC was organized as a wholly owned subsidiary of Southern Union in 1953 and remains such to date.

From the year 1950 to the present, the Tribe has been lessor and royalty-interest owner of oil and gas leases approved by the Secretary of the Interior on the Tribe's Reservation lands in the San Juan Basin. The leases which are the subject of this litigation are Jicarilla Lease Nos. 10, 47, 100, 101, 103-107, 145, 150, 153, 397 and 416-18. In 1950, SUG became the original lessee of leases numbered 10, 100, 101, 103 through 107, 145, 150 and 153. On May 20, 1952, SUG assigned separate undivided one-half interests in leases 104 and 107 to Humble Oil Company (Exxon). On January 1, 1956, Exxon contracted to sell natural gas produced from leases 104 and 107 to SUG. Sales of natural gas continue to be made pursuant

to this contract, as amended, to date. Exxon assigned its undivided one-half interest in lease 107 to Billy J. Knott effective February 9, 1973, reserving all lease hold rights below the base of the Dakota formation. Exxon's conveyance to Knott was approved by the Bureau of Indian Affairs (BIA) in May of 1979, effective retroactive to the date of conveyance.

On January 1, 1955, SUG assigned separate undivided one-half interests in leases 100, 101, 103, 105, 106, 145, 150 and 153 to Aztec, at that time a wholly owned subsidiary company of SUG. Aztec acquired leases numbered 397 and 416 through competitive lease sales in 1966 and 1969 respectively. Aztec and Southland have sold natural gas produced from their leases to SUG pursuant to a gas purchase contract executed December 12, 1953, as amended. On January 1, 1961, SUG assigned its rights in leases 10 and 47 and separate undivided one-half interests in leases 100, 101, 103-107, 145, 150 and 153 to Supron, at that time a wholly owned subsidiary of SUG. On that same date, Supron executed a gas purchase contract with SUG for sale of natural gas from the leases assigned to it. Two additional gas sales contracts were executed between Supron and SUG regarding sales from additional properties previously owned by SUG assigned to Supron. Supron acquired leases 417 and 418 through competitive lease sales in May of 1969. Numerous additional gas contracts have been evidenced throughout these proceedings but need not be particularly delineated here. Suffice it to say that the numerous dealings between and among the defendant energy companies and others have been commensurate with the complexities generally associated with the oil and gas industry.

The contractual relations of the Tribe and defendants-lessees are governed by the provisions of Standard Lease Form 157 entered into on behalf of the Tribe by the Secretary pursuant to federal statutes, 25 USC 396(a) *et seq.*, and federal regulations, 25 CFR Part 171 and

30 CFR Part 221. Under the terms of the lease and the applicable federal statutes and regulations, the Secretary has the duty and the jurisdiction to determine whether lessees are performing according to the terms and conditions of leases on Indian lands and to determine the "value" of any minerals produced for purposes of computing royalties to be paid by the lessees.

Prior to its institution of this action, the Tribe demanded in 1973 that the Secretary take appropriate and necessary action to make determinations required of him under the terms of the lease and to require lessees to perform their obligations as denominated in the lease provisions. The Tribe has continued to demand action of the Secretary since 1973. When it became clear to the Tribe that, in its opinion, its demands would not be heeded by the Secretary, it instituted this action in 1975. In addition to its demands on the Secretary, the Tribe has previously demanded of defendants-lessees that they pay royalties on gas produced based on the actual value of such gas, that they account separately for liquid hydrocarbon substances as required by the lease terms, that they drill such offset well as are necessary to protect lease lands from drainage, and that they exercise reasonable diligence in the development of oil and gas, while products can be secured in paying quantities, of leases held by these lessees on Reservation lands. The Secretary has assigned responsibility for the leases in question to the Area Oil and Gas Supervisor of the United States Geological Survey (USGS) who has been stationed at various times in Roswell and Albuquerque, New Mexico and Durango, Colorado.

THE TRIBE'S ANTITRUST CLAIMS

The Tribe's antitrust claims are several. It claims Supron monopolized the market for liquid hydrocarbons in restraint of trade and in violation of Section 1 of the Sherman Antitrust Act, 15 USC 1, in light of Supron's

operation of the Lybrook Gasoline Extraction Plant from 1971 to 1976. It claims that the contract agreement entered into between Supron and SUG unlawfully fixed the price of liquid hydrocarbons in restraint of trade; that Southland and SUG unlawfully fixed the price of natural gas pursuant to gas purchase contracts effected between them on December 31, 1953 and January 2, 1954; that Supron and SUG unlawfully fixed the price of natural gas in restraint of trade pursuant to the gas purchase agreement effected betwen them on January 1, 1961; that Supron, SUG and SUGC fraudulently concealed from the USGS and the Tribe the amount of actual revenues received for gas and associated liquid hydrocarbons produced therefrom, which concealment amounted to a conspiracy in restraint of trade and in violation of the Antitrust Acts; that Supron, Southland and Exxon conspired to fraudulently fail to accurately account for liquid hydrocarbons between 1973 and 1975 as required by the terms of the leases; and that Supron and Southland and Supron and Exxon respectively conspired in restraint of trade in 1975 and 1976 by failing to diligently develop the leases or drill offset wells required by the terms of the leases and in fraudulently concealing from the USGS and the Tribe the development potential of the leases in order to hold the properties which were the subject of the leases for speculation.

Plaintiff further directs a claim of conspiracy in restraint of trade against Supron and SUG in that these defendants prevented the Tribe from taking its royalty gas in kind as provided under the terms of the leases. An additional claim of conspiracy to fix prices is lodged against SUG, SUGC and Supron based on their June, 1976 settlement agreements which resulted in the dismissal with prejudice of State Court cases brought in Texas and New Mexico concerning the price to be paid for natural gas produced from leases on the Reservation. Finally, plaintiff claims that at various times until 1976, defendants Supron, SUGC, SUG and Aztec, violated Sec-

tion 8 of the Clayton Antitrust Act, 15 USC 19, which prohibits interlocking directorates of competing companies when the potential for antitrust violations by those companies exists.[1]

Subject matter jurisdiction over antitrust claims resides in a federal District Court on a finding that the activities which form the basis for alleged antitrust violations are in or affect interstate commerce. *Hospital Building Co. v. Trustees of Rex Hospital*, 425 U.S. 738 (1976). In my Memorandum Opinion dated April 13, 1979, I concluded, in denying defendants' motions for summary judgment, that plaintiff had made sufficient showing of the required nexus between interstate commerce and the acts forming the basis of the alleged antitrust claims to withstand defendants' motions for summary judgment. I conclude from facts adduced at trial that the activities of defendants which form the basis for plaintiff's antitrust claims sufficiently affect interstate commerce to provide subject matter jurisdiction over plaintiff's antitrust claims. I find further from facts adduced at trial that the Tribe is a natural gas producer and therefore a competitor in the sale of natural gas.

The relevant geographical market in which to view plaintiff's antitrust claims is the San Juan Basin of Northern New Mexico, a discrete oil and gas producing region. The relevant product which is the subject of plaintiff's antitrust claims is natural gas, including natural gas sold intrastate and interstate. As to plaintiff's claim of monopoly regarding the operation of the Lybrook plant, the relevant market is liquid hydrocarbons processed from natural gas marketed both intra-and interstate.

Plaintiff's claim of monopoly may be dispensed with briefly. Quite simply, the Tribe has failed to adduce proof

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[1] Plaintiff's belated claim of price discrimination in violation of Section 2 of the Clayton Act, 15 USC 13, was raised and withdrawn, both after trial on the merits.

sufficient to sustain a claim of monopoly. Whether the relevant market is intrastate or interstate sales of liquid hydrocarbons, neither Supron nor SUG ever marketed more than 50% of the liquid hydrocarbons sold in the San Juan Basin. Having never acquired more than one-half of the relevant market in liquid hydrocarbons in the San Juan Basin, neither Supron nor SUG, as a matter of law, ever acquired a large enough proportion of the market to sustain plaintiff's claim of monopoly. *Continential Baking Co. v. Old Homestead Bread Co.*, 476 F2d 97, 104 (10th Cir.), cert. den., 414 US 975 (1973); *United States v. Aluminum Co. of America*, 148 F2d 416, 424 (2d Cir. 1945). The Tribe's claim of monopoly violation will be dismissed with prejudice.

The Tribe's claim of conspiracy in restraint of trade to prevent it from taking its royalty gas in kind may be dismissed in terms equally brief. The leases at issue in this action expressly require the Tribe to give thirty days written notice of its intent to take royalty gas in kind. Standard Lease Form 157, ¶ 4(c). The Tribe presented no evidence that at any time it presented adequate notice to its lessees to take its royalty gas in kind. Whether the Tribe thought it could take its gas in kind or whether lessees would have acquiesced to such a demand from the Tribe is immaterial in the absence of the required written notice. Additionally, defendants were under no affirmative obligation to indicate to the Tribe whether they believed that contractual obligations with third parties prevented the Tribe from taking its royalty gas in kind. Absent a formal request from the Tribe, defendants had no such affirmative obligation.

Plaintiff's further claim of conspiracy in restraint of trade to limit development of the leases and to fraudulenty conceal the potential of the leases fails in light of substantial evidence that defendants-lessees acted and informed the USGS of their intentions when requested to do so based on sound, if conservative, business decisions.

Several of the leases in issue involved interests held jointly by lessees. That joint lessees might have communicated between themselves regarding decisions concerning development and potential of the leases necessarily followed from the jointly held rights and concomitant obligations of joint lessees. I find in the record no evidence of any concerted agreements among lessees to defraud or conceal from the USGS and the Tribe information regarding the leases or lessees' intentions concerning the leases.

Lessees' responses to USGS inquiries regarding development and potential of the leases were at all times honest, if not unequivocal. That joint lessees considered carefully the content of their responses to USGS inquiries resulted not from conspiratorial intent but rather from the real or apparent fear that incorrect or insufficient responses would place their valuable leaseholds in jeopardy. Defendants cannot be faulted for responding as they did. Whether or not they may have agreed with the USGS' position regarding their leases, defendants felt obliged to grant the USGS some degree of deference in order to protect their leasehold interests.

Plaintiff's claims of conspiracies to fix prices and to limit development of the leases based on the gas purchase contracts entered into by defendants is similarly unpersuasive. Substantial evidence at trial revealed that the long-term contracts executed in the San Juan Basin had been the order of business since the 1930's. Life of the lease contracts and long-term twenty-year contracts were deemed required by both purchasers and buyers of natural gas in the San Juan Basin. Buyers found them necessary because of the substantial commitment required to develop production and transportation facilities sufficient to service wells in remote areas of Northern New Mexico and sellers because of the need to insure a constant, stable market for their production even, as in later years, when wells became substantially depleted and thereby less valuable producers. The comparable terms and prices set in

these contracts reflect not illegal conspiracies but rather the considered judgment of the parties to these contracts that such prevailing terms and prices, at the time these contracts were consummated, were fair and reasonable to all parties.[2]

Similarly, the presence of favored nation clauses[3] in the gas purchase contracts under attack are incompatible with a conclusion that there existed conspiracies to fix prices and restrain trade. To the contrary, favored nation clauses insured that higher prices received by other sellers as a result of subsequent contracts would be afforded to signatories to the earlier contracts. The favored nation clauses guaranteed a continuing escalation of prices received by lessees and thereby increased royalties received by the lessor, contrary to any claim that a conspiracy existed to fix prices below market value in the Basin. The Tribe's claim that SUG was able to avoid triggering these favored nation clauses by calling on gas reserves it controlled in other markets points not to conspiracy but to business maneuvering of which SUG was able to take advantage in order to deliver its product to its customers at the lowest possible price. In any event, SUG was not able uniformly to avoid price escalations due to favored nation clauses. These clauses were triggered from time to time.

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[2] While evidence revealed that SUG tended to negotiate gas purchase contracts on a "take it or leave it" basis with regard to prices dictated by it, this at best tends to reveal monopolistic activities attributable not to defendant-lessees, but to SUG, who has bought its peace in this lawsuit. This apparently illegal activity on the part of SUG cannot be imputed to the defendants remaining in this action.

[3] The favored nation clause (also known as a most favored nation clause or price equalization clause) provides that the seller will receive a price for gas produced no less than that paid by the buyer to any other natural gas producer in the Basin for natural gas delivered under similar conditions, quality, volume and pressure.

Testimony at trial established that the natural gas purchase contracts attacked by the Tribe were "typical wellhead gas purchase contracts," as was a contract effected between the Tribe and SUGC in December, 1976. The Tribe received an identical price for its natural gas in its 1976 gas purchase contract, which contract included identical escalation clauses to those found in the several purchase contracts under attack. Evidence at trial also indicated that low prices for natural gas in the 1970's resulted in part from federal regulations concerning interstate gas prices and actions taken by the New Mexico Public Service Commission.

The Tribe also claims that SUG dealt with its subsidiaries differently than with independent producers in that its subsidiaries received life of lease contracts as opposed to the twenty-year term contracts received by independent producers. No substantial difference existed between the two. In terms of the twenty-year contract, depletion of the lease after twenty years was so great that no new purchaser would consider negotiating a contract on the lease. In effect, then, a renegotiation of the twenty-year lease by the same parties virtually always would occur. In conclusion, I find that the natural gas purchase contracts which form the basis for plaintiff's claims of conspiracy to fix prices in restraint of trade were arms-length contracts negotiated between purchaser and seller which did not restrain trade, did not fix prices and did not amount to illegal conspiracy.

Plaintiff's claims of conspiracies based on fraudulent concealment of the actual revenues received for gas and liquid hydrocarbons and for failure to accurately account for liquid hydrocarbons according to the terms of the

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[4] This finding applies as well to plaintiff's claim based on the settlement between Aztec and SUG of the State Court cases mentioned above. The price SUG agreed to pay, $.676 per mcf, BTU-adjusted, was nearly the seventy cents sought by Aztec in its Dallas County petition.

leases fails on the basis of the stipulation entered into by counsel at trial. It was stipulated that defendants-lessees accurately reported to the USGS volumes of gas produced from the Tribe's leases, that they correctly reported to the USGS the consideration received by them for the sale of that production to SUG and that they paid to the Tribe, or more accurately to the Secretary on behalf of the Tribe, royalties at the appropriate rate, as that rate was determined by the leases terms, based on such reported production and sales revenues. (Transcript, Volume VII, 7). It is acknowledged that plaintiff makes the additional claims that defendants have at various times failed to pay royalties based on a dual accounting method, being the higher of a BTU-adjusted or net realization method,[5] on gas produced and that the Secretary has failed to accurately determine the correct basis on which royalties were to have been paid to the Tribe. These claims however do not raise the specter of antitrust violations but rather concern plaintiff's common law claims against defendants-lessees for breaches of the leases and against the Secretary for breach of his fiduciary duty.

Plaintiff has failed to establish its consipracy claims under the antitrust laws by a preponderance of the evidence and they will therefore be dismissed with prejudice.

At trial, plaintiff raised its claim that certain of the defendant energy companies in the past had interlocking directorates in violation of Section 8 of the Clayton Antitrust Act, 15 USC 19. A Section 8 violation exists when two or more corporations, one with a net worth in excess of one million dollars, who are competitors such

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[5] The BTU-adjusted method of accounting requires that the base price for gas produced be adjusted upward or downward according to the heating value of such gas. The net realization method of accounting involves a determination of the value of component parts of the gas stream derived by processing gas through a gasoline extraction plan, with allowance made for the cost of manufacturing such component parts.

that any agreement between the companies might constitute a violation of the antitrust laws, share a common director. *Protectoseal Co. v. Barancik*, 484 F2d 585, 589 (7th Cir. 1973); 15 USC 19. *See also, United States v. Sears, Roebuck & Co.*, 111 F.Supp. 614 (S.D.N.Y. 1953). Relief, as well as standing to sue, is predicated on a claim of injury of the sort contemplated by the antitrust laws. *Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc.*, 429 U.S. 477, 489 (1977). Relief may include injunctive relief pursuant to 15 USC 26 and treble damages under 15 USC 15. A corporation is subject to suit under Section 8. *SCM Corp. v. Federal Trade Commission*, 565 F2d 807, 811 (2d Cir. 1977), cert. den., 434 U.S. 1086 (1978).

Alleging antitrust injury based on the claimed Section 8 violation, plaintiff has standing to sue under 15 USC 15. Because plaintiff's claim is one for damages and not for injunctive relief, *see*, Plaintiff's Amended Proposed Findings of Fact and Conclusions of Law, at 33, ¶ 31, the issue of mootness so often associated with Section 8 litigation is not present in this law suit. *See, e.g., United States v. W. T. Grant Co.*, 345 U.S. 629 (1953); *SCM Corp. v. Federal Trade Commission*, 565 F2d at 812.

Plaintiff bases its claims on at least three separate violations of Section 8.[6] In 1972, Supron and SUGC had common directors. From 1972 to 1975, Aztec and Supron had common directors. From time to time including 1976, SUG, SUGC, Supron and Aztec all had at least one common director. At all times during which they had common directors, these companies were competitors in the sale of natural gas. The elimination of competition by agreement between any of these companies might have constituted a violation of the antitrust laws. At all times during which these companies had common directors,

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[6] A fourth claimed violation involves only SUG and SUGC who are no longer parties defendant in this action. Their absence renders this fourth claim immaterial.

Supron, Aztec and SUG each had net worth in excess of one million dollars. Plaintiffs, therefore, have proved technical violations of Section 8 of the Clayton Antitrust Act. However, having found above no substantive violations of the antitrust laws as claimed by plaintiff, and finding that these technical violations of Section 8 without more caused no injury to plaintiff, and in light of the fact that plaintiff seeks not injunctive relief but damages against these defendants, I conclude that plaintiff's claims under Section 8 of the Clayton Antitrust Act should be dismissed. *Gottesman v. General Motors Corp.*, 436 F2d 1205, 1210 (2d Cir.), cert. den., 403 U.S. 911, reh. den., 404 U.S. 876 (1971).

THE TRIBE'S COMMON LAW CLAIMS

Plaintiff claims that defendants-lessees have breached the terms of the several leases which are the subject matter of this litigation. The Tribe claims that lessees have failed to diligently develop their leaseholds, have failed to drill offset wells to protect the leases from drainage, have failed to accurately account for royalties based on production from the leases and have failed to account for liquid by-products and royalties thereon produced from natural gas extracted from wells on the leases. Defendant Secretary of the Interior is charged with a breach of his fiduciary duty in failing to take appropriate action to make determinations necessary under the lease terms and to require the lessees to perform their obligation as set out in the lease terms.

Diligent Development

The rule to be applied concerning plaintiff's claim of failure to diligently develop the leases is one of New Mexico law. *Clayton v. Atlantic Refining Co.*, 150 F. Supp. 9 (D.N.M. 1957). The law of New Mexico embraces the "prudent operator" rule. *Id.*, at 16. Under the prudent operator rule, a lessee is held to act in a manner

which "would be reasonably expected of operators of ordinary prudence, having regard to the interests of both lessor and lessee . . . ." *Brewster v. Lanyon Zinc Co.*, 140 F. 801, 814 (8th Cir. 1905). What is required of an operator-lessee must be determined on a case by case basis giving due consideration to the totality of the circumstances. *Sun Oil Co. v. Frantz*, 291 F.2d 52, 55 (10th Cir. 1961). An alternative formulation of the rule indicates that a lessee must continue to develop a lease if there is an expectation of finding gas without undue risk as well as an expectation of a payout within a reasonable time. What is to be considered a reasonable time varies with the circumstances. *Id.*, at 54-55.

Expert testimony at trial revealed a general consensus that a well may be considered economical to drill if preliminary studies indicate a three to one return on investment within three to four years of commencement of the well. Testimony further revealed a genuine difference of opinion, both between plaintiff's experts and defendants' experts and between experts testifying on behalf of the several defendant-lessees, as to the economics and prognosis for drilling any particular well based on geologic and economic considerations available to all of them. Significantly, the differences of opinior between defendants' experts indicated that some leeway must be given to each individual operator's decision to drill or not to drill particular wells on the leases. And while an operator is charged with the duty of having due regard for the interests of the lessor as well as itself, the lessee is not obliged to pursue development when, in its sound economic judgment, drilling such a well would result in minimally positive or negative economic results for itself.

To exemplify this concept, it is the Tribe's position that Exxon, as operator of Jicarilla Lease 104, should have drilled an additional one to three wells to the Gallup formation as of January 1, 1976. Exxon's response indi-

cated that the wells presently on Lease 104 would recover substantially all the recoverable reserves in the Gallup formation and that while additional wells would increase the Tribe's royalty values initially by virtue of increased production, additional wells would also decrease the project life in the Gallup formation substantially. Additional wells, of course, would require significantly additional investment by the operator and according to Exxon's economic analysis, would actually decrease total profits both for Exxon and for the Tribe in the long run. Under these circumstances, Exxon cannot be said to have failed to diligently develop the lease in question.

The most important factor in determining whether the lessees have diligently developed the leases in question is the price of gas at any time at which it is claimed additional wells should have been drilled. By circumstance, the price of gas has increased dramatically from 1975 to date and according to all economic indicators, should continue to do so in the near future. It was the uniform response of defendants-lessees' experts at trial that additional wells proposed by plaintiff's experts were not economical in the years plaintiff claims they should have been drilled. This was as a result of the prices of gas prevailing at the time and the long payout period which would have been required based on those prices. Defendants' experts admitted that most of the wells proposed by plaintiff's experts either had in fact been drilled at times later than those proposed by plaintiff's experts or are included in defendants' proposed drilling programs for the near future. Defendants' experts attributed the inclusion of these many wells in their drilling programs to the significant and dramatic increase in the price of gas to date.

An additional factor in determining whether or not to drill is the geologic information available on which to base a reasoned decision as to whether drilling at any particular location will result in a well producing in pay-

ing quantities. Here too opinions differed as to whether the geologic information available suggested success or failure in developing producing wells at given locations. I find that defendants' decisions not to drill certain locations based on the geologic data available were informed and sound, if not always in agreement with the conclusions reached by plaintiff's experts. The fact that from time to time certain companies elected to go non-consent [7] on a well within a jointly held lease indicates further that agreement, even among producers in partnership, was not always the case.

After an extensive review of the record, I conclude that plaintiff's claim that defendants have failed to diligently develop the leases in question is not well taken. Defendants have proceeded to develop these several leases according to sound economic business principles. While the criteria established by defendants concerning the economics of any particular individual well are admittedly conservative, the speculative nature of the oil and gas business may in fact require that conservatism temper and inform sound business decisions. Defendants cannot be faulted for proceeding in such a manner.

Moreover, the recent inclusion of several wells proposed by plaintiffs in defendants' drilling programs indicates that defendants heretofore have decided not to drill these wells based on sound economic principles and not for speculative purposes as was claimed by the plaintiff. Indeed, defendants' experts testified that in spite of the almost certain price spiral in the natural gas market which of course will yield higher prices for gas from wells

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[7] Non-consent indicates the unwillingness of a joint lessee to share in the risk of any particular drilling operation. The joint lessee who drills does so at his own risk. If production is secured, the non-participating lessee suffers a financial penalty to the benefit of the lessee who drilled before being permitted to share in the proceeds of well production. *See, e.g.*, Supron Exhibit SUP 11, Joint Operating Agreement, Article 10, at 6.

commenced later rather than earlier in time, defendants intend to drill wells as soon as economic indicators suggest it will be profitable to do so. The need for continued cash flow, a requirement for any business organization, was cited, and is deemed acceptable, as the reason for such activity.

An additional observation must be made on plaintiff's claim of defendants' failure to diligently develop these leases. In counterpoint to plaintiff's insistence that it would have preferred to take royalties on gas produced at the lesser prices prevailing in the mid-1970's in order to utilize the cash in hand at that point in time, defendants have insisted steadfastly that because of the dramatic rise in gas prices, future production of the reserves remaining under these leases will produce royalties to the Tribe far in excess of royalties which would have accrued had the leases been more fully developed earlier.[8] Without question, there is merit to both arguments. The Tribe, one of a people historically impoverished relative to its more recent neighbors, certainly would have benefited from revenues accruing in the mid-1970's. On the other hand, testimony revealed that the Tribe will receive substantially higher revenues presently and in the near future as the result of the defendants' decisions to wait to develop the leases in question. Plaintiff's claim that such a conclusion is based on speculation and cannot be relied on flies in the face of the reality of the marketplace. While I am bound to my courtroom, my observations on such imposing realities as the rising price of gas are not.

Suffice it to say that the law of diligent development permits the lessee to consider its own economic well-being in addition to that of the lessor. Given the known sub-

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[8] The evidence indicated this would be the case even assuming a rate of return of 20% annually on royalties accruing to the Tribe from 1971 through 1980.

stantial reserves underlying Reservation lands, the Tribe would appear to have been in a position to negotiate the acquisition of substantial capitalization needed for its desired projects by pledging future royalty revenues, sizeable in amount and prolonged in time, as collateral for whatever commitments it might have sought to make. To require operators to develop leases earlier than might be economically indicated, albeit according to the economics derived by the operator, so that the lessor might have cash revenues at the earliest time possible, is a result not required by the prudent operator rule.

Substantial evidence was adduced at trial regarding the Secretary's role in defining the concept of diligent development insofar as it pertains to the Jicarilla Tribe's leases. Representatives of the USGS testified that no guidelines for diligent development existed prior to the issuance of the Davenport Memorandum [9] except for the requirements that a lease produce within its primary term and that drainage of a lease be prevented by requiring the drilling of offset wells. The Davenport Memo itself would appear to indicate that development of leases on Indian lands has been left largely to the considered judgment and discretion of lessees, primarily to avoid duplication of effort by lessees and the severely understaffed offices of the USGS in the Southern Rocky Mountain Region.

From a practical viewpoint, Ms. Davenport's conclusion would appear to be reasonable. However, the Secretary has obligated himself and his governmental representatives to the most exacting standards required of a fiduciary of an Indian Tribe. *Seminole Nation v. United States*, 316 U.S. 286, 296-7 (1942). Limited financial resources cannot excuse the Secretary from his strict

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[9] The Davenport Memorandum, promulgated by Ms. Joan M. Davenport, Assistant Secretary of the Interior, in response to my September 7, 1978 Order, was made of Record March 12, 1979.

fiduciary obligation to oversee leases on Indian lands and insure that lessees comply completely and timely with the terms thereof.

The Secretary may well have placed himself in a hopeless situation having bound himself to the standards of a fiduciary without the resources to satisfy those obligations. Directives have been set out in Ms. Davenport's memorandum and additionally in a memorandum to conservation managers of the Central, Eastern and Western Regions from the Acting Chief of the Conservation Division of the USGS subsequent to and in light of Ms. Davenport's memorandum, *see*, Government Exhibit G-35, purporting to establish guidelines concerning diligent development on Indian oil and gas leases. Whether these in fact comport with the concept of diligent development as that term has meaning in law is not an issue in this law suit. Accordingly, I decline to comment on those guidelines. What is in issue in this law suit, however, is the Tribe's claim that the Secretary has failed to satisfy his fiduciary duty to the Tribe under the leases.

I find that, notwithstanding the unique and extensive effort given by the USGS to monitoring the Tribe's leases and defendants-lessees' adherence to the terms therein,[10] the Secretary has breached his fiduciary duty to insure for the Tribe that its lessees have complied with the term of the leases which requires diligent development. It is not that the Secretary has provided too little in terms of satisfying his fiduciary duty but that it has come too late. That defendants have, in my opinion, diligently developed the leases is fortuitous and did not result from timely action taken by the Secretary.

Notwithstanding my conclusion above that defendants-lessees have not failed to diligently develop the leases in

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[10] The Jicarilla Response Committee, formed in 1974 within the USGS Southern Rocky Mountain Regional Office in response to the Tribe's demands, spent approximately 1,200 man-hours investigating the Tribe's claims under the leases.

question, I find that the Secretary and his named representatives have failed to adequately monitor development of these leases sufficiently to insure compliance with the terms thereof. A declaratory judgment to this effect will be entered, and should it appear that the Secretary is unable or unwilling to comply with his fiduciary obligations on behalf of the Tribe, injunctive relief may be appropriate.

Offset Wells

Plaintiff claims, as a further breach of the leases, that defendants have failed to drill offset wells to protect drainage from leased lands and that the Secretary's failure to require such offset wells is yet another breach of his fiduciary duty under the leases. Regarding the general obligation under the leases to protect from drainage by drilling offset wells, I adopt the discussion in Section I-A of the Davenport Memorandum and incorporate it herein.

The leases which plaintiff claims are subject to drainage are numbers 101 and 150, both of which are held jointly by Supron and Southland. Following issuance of the Davenport Memorandum, USGS employee David Maldonado investigated the claims of possible drainage on these leases, concluding that they were not subject to drainage by the adjoining leases identified in the Davenport Memorandum and relied on by plaintiff. I find Maldonado's testimony to be competent and credible and therefore conclude that no drainage is occurring on leases 101 and 150 which requires the drilling of offset wells.

Although the USGS acted quickly and industriously in response to the memorandum of Ms. Davenport with regard to offset wells, I find that absent an order of this Court requiring the Secretary to make a determination regarding the question of drainage of leases on the Tribe's Reservation, such inquiry would not have been made. Accordingly, I conclude that the Secretary has

breached his fiduciary duty under the leases to insure, on behalf of the Tribe, the protection of leased lands from drainage by requiring the drilling of offset wells. As was the case on the issue of diligent development, a declaratory judgment will enter to this effect, and injunctive relief, should it prove necessary, may be appropriate.

Value

Plaintiff's claims on the issue of value are again two-fold. It claims that defendants-lessees have breached the terms of the several leases by failing to accurately account for value per the lease terms. Plaintiff seeks an accounting and damages on the basis of the claimed breaches. The plaintiff also lodges a claim against the Secretary to the effect that he has failed to accurately determine value according to the lease terms for the purpose of computing royalties to the Tribe. Plaintiff seeks declaratory judgment that the Secretary has breached his fiduciary duty to accurately account and to require defendants-lessees to account for and pay royalties according to the lease terms. By such a declaratory judgment the Secretary would be obliged to require defendants-lessees to accurately account for and pay any additional royalties due under the lease terms.

Partial summary judgment on the issue of value was granted to defendants by my Order of September 7, 1978. In that same Opinion and Order, I deferred ruling on the motion for summary judgment on the issue of dual accounting pending resolution of administrative proceedings then, and now, pending. In a subsequent Memorandum Opinion and Order dated December 19, 1978, I denied plaintiff's motion to reconsider the grant of summary judgment on the value issue. In my Memorandum Opinion and Order dated April 19, 1979, I stated that if at trial plaintiff established that the Secretary's computation of value was based on fraudulent information

and therefore was clearly erroneous, I would consider my ruling on the issue of value.

It has become clear, on review of the Record, that my summary judgment ruling on the issue of value was incorrect based on factors other than the alleged fraud perpetrated on the Secretary. Fairness and justice require that I right wrongs when it is in my power to do so. Revision of prior rulings in this action is within the scope of my authority. Fed.R.Civ.P. 54(b). Defendants had the opportunity to brief the value issue prior to my ruling on summary judgment. By moving for summary judgment, defendants acknowledged the absence of any genuine issue as to any material fact. Fed.R.Civ.P. 56 (c). That state of affairs has not changed in the interim. Accordingly, I am free to revise my ruling on the issue of value and also my statement that reconsideration would follow only if proof of fraud was adduced at trial.

I find, on the basis of the stipulation entered into by counsel at trial, that defendants accurately reported the volumes of gas produced from the leases and the prices received on sales of such gas at the wellhead and that defendants accurately paid royalties based on the volumes and prices reported to the USGS. Such a finding, however, does not answer the question whether defendants-lessees paid royalties to the Tribe in the amount to which it was entitled under the lease terms and the federal regulations which inform them. *See*, Standard Lease Form 157, ¶ 3(c); 30 CFR §§ 221.46-.47, 221.50-.52.[11]

If the Secretary has breached his fiduciary duty because the method by which he computed royalties did not derive for the Tribe the highest royalties payable under the lease terms and the federal regulations, or because

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[11] 25 C.F.R. § 171.13(a) also speaks to royalty rates under Tribal oil and gas leases, but only to reiterate the express terms of ¶ 3(c) of the lease.

he has failed to accurately account or require defendants-lessees to account according to the lease terms, then the defendants have in fact breached the terms of the lease, albeit through no apparent fault of their own. What is required to determine whether the Secretary has in fact breached his fiduciary duty to the Tribe is inquiry into the relevant lease terms and federal regulations, since the Secretary's obligation to the Tribe is necessarily defined therein.

Defendants-lessees' insistent claim throughout these proceedings on the issue of value has been that the Secretary in his discretion accepted "[t]he actual amount realized by the lessee from the sale of said products" as "conclusive evidence" of value for the purpose of computing the Tribe's royalties. Lease, *supra* at ¶ 3(c). Indeed, the fact that the Secretary in his discretion was authorized by the lease term to accept sales price as "conclusive evidence" of value was the basis for granting summary judgment on this issue in September, 1978 and denying plaintiff's motion to revise in December, 1978. Notwithstanding my conclusion then, it is my conclusion now that the Secretary's fiduciary obligation to the Tribe necessarily circumscribes the discretion granted him by the lease terms should it be determined that the two are in conflict.

The relevant term of the lease provides:

> 3. . . . [T]the lessee hereby agrees:
>
> (c) Rental and royalty.—To pay, . . . a royalty of 12½ percent of the value or amount of all oil, gas, and/or natural gasoline, and/or all other hydrocarbon substances produced and saved from the land leased herein . . . . "[V]alue" for the purposes hereof may, in the discretion of the Secretary, be calculated on the basis of the highest price paid or offered . . . at the time of production for the major portion of the oil of the same gravity, and gas, and/

> or natural gasoline, and/or all other hydrocarbon substances produced and sold from the field where the leased lands are situated, and the actual volume of the marketable product less the content of foreign substances as determined by the oil and gas supervisor. The actual amount realized by the lessee from the sale of said products may, in the discretion of the Secretary, be deemed mere evidence of or conclusive evidence of such value. . . . It is understood that in determining the value for royalty purposes of products, such as natural gasoline, that are derived from treatment of gas, a reasonable allowance for the cost of manufacture shall be made, such allowance to be two-thirds of the value of the marketable product unless otherwise determined by the Secretary of the Interior on application of the lessee or on his own initiative, and that royalty will be computed on the value of gas or casinghead gas, or on the products thereof (such as residue gas, natural gasoline, propane, butane, etc.), whichever is the greater. Standard Lease Form 157, ¶ 3(c).

In its simplest terms, the lease provides that royalty is based on the value of gas. Value is based on the price and the volume of gas produced. According to the lease term, value can be computed any number of ways. Sales price is one basis for determining value and clearly the most expedient for the purpose of computing royalties. Value based on sales price is determined at the point of sale, *Kretni Development Corp. v. Consolidated Oil Corp.*, 74 F2d 497 (10th Cir. 1934), cert. den., 295 U.S. 750 (1935), in this case at the wellhead. Value (price times volume) can be computed on the gas stream as a whole, e.g., at the wellhead, or on the component parts of the stream, e.g., at the tailgate of a gasoline extraction plant. Value of component parts, when added together, produce

aggregate value on which to compute royalties.[12] Hydrocarbon substances proceeded through a gasoline extraction plant and sold at the tailgate take the form of liquids, or liquid by-products of the gas, and residue gas. When gas is processed into component parts, the lease and the regulations require that value of the component parts be determined and then compared to the value of the gas stream as a whole (being volume times either sales price or "highest price paid or offered . . ."). Royalties are to be paid on whichever is the greater. Lease, *supra* at ¶ 3(c); 30 C.F.R. §§ 221.47, .50.

This standard lease has attempted to provide contingent bases for computing royalties in light of the various alternative methods by which gas may be produced and sold. The last sentence in paragraph 3(c) applies when gas produced from the lease is subject to "treatment," as when it is processed through a gasoline extraction plant. Two provisions are set out in that final sentence. The first states that

> . . . in determining the value for royalty purposes of products, such as natural gasoline, that are derived from treatment of gas, a reasonable allowance for the cost of manufacture shall be made . . . .

The second states that

> . . . royalty will be computed on the value of gas or casinghead gas, or on the products thereof (such as residue gas, natural gasoline, propane, butane, etc.), whichever is the greater.

This latter provision requires that the Secretary, or the lessee, determine the value of both unprocessed gas, e.g.,

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[12] Determining aggregate value may also be required at the wellhead if liquids are separated there by mechanical means. Plaintiff makes no claim in this case that royalties on liquids separated at the wellhead have not been properly reported and paid. It is important to note, however, that a determination of aggregate value may be required elsewhere than at the tailgate.

gas or casinghead gas, and processed gas, e.g., residue gas and liquid by-products. Determining value of proccessed gas necessarily requires a determination of the aggregate value of the products of the various hydrocarbon substances recovered through processing, taking into account the cost of manufacturing allowance provided for in the lease.

The regulations contemplate this application of the net real method of accounting. 30 C.F.R. § 221.50 provides:

> (a) *Royalty accrues on dry gas,* whether produced as such or as residue gas *after the extraction of gasoline.*
>
> (c) . . . for the purpose of computing royalty *the value of wet gas* shall be either the *gross proceeds accruing to the lessee* from the sale thereof or *the aggregate value* determined by the Secretary *of all commodities,* including residue gas, obtained therefrom, *whichever is greater.* (emphasis supplied).

The regulations, based on the lease term, require the Secretary to make two comparisons. He must compare sales price with the value of production on gas produced at the wellhead, and sales price with value by the net realization method of accounting when residue gas and liquids are produced at the tailgate of a gas plant. 30 C.F.R. §§ 221.47, .50(a), (c). Royalties are computed on the higher of the two values derived from these two comparisons. *Id.*

Defendants argue that because they do not operate such a gas plant (Supron does not ascribe to this argument for the years 1971-6, nor could it) they are not obliged to account by net real method and that when gas is sold at the wellhead, value, based on sales price, is determined there. The explicit terms of the regulations indicate that unlike value based on sales price, value based on net real accounting is not tied to the point of sale. *Id.* The cases cited by defendants are not to the

contrary. The lease terms addressed in those cases differed from those at issue here in that they provided fewer alternative methods by which to calculate value. *See, Barby v. Cabot Corp.*, 465 F2d 11, 13 n.1 (10th Cir. 1972); *Kretni Development Corp. v. Consolidated Oil Corp., supra. Compare Matzen v. Hugoton Prod. Co.*, 321 P2d 576, 582-3 (Kan. 1958); *Phililps Petroleum Co. v. Johnson*, 155 F2d 185, 188-9 (5th Cir.), cert. den., 329 U.S. 730 (1946). It is important to note that neither of the two provisions in the last sentence of paragraph 3(c) is limited to circumstances where the "treatment of gas" is done by the lessee or at his discretion. The net realization method of accounting, described by the second provision of this last sentence of paragraph 3(c), is required of any lessee who produces gas which is later processed into component products. Gas produced from the Jicarilla leases was processed into component parts through the Lybrook Gasoline Extraction Plant.

I conclude that where, as here, gas produced from the lease is processed into component products, dual accounting is required by the terms of the lease. Accordingly, the Secretary had the obligation to require defendants-lessees to account on the net realization method. Defendants-lessees never accounted for gas produced from the leases on the net realization method, nor were they required to do so by the Secretary. Because the Secretary failed to implement this requirement of dual accounting, he has failed to accurately account for value according to the terms of the lease.

El Paso Natural Gas Company (El Paso) has paid producers for natural gas on a BTU-adjusted basis for some time, at least since as early as 1965. Pursuant to an agreement settling prior claims entered into between El Paso and the Tribe, El Paso has reported voluntarily by a dual accounting method for some time. El Paso's agreement to dual account, arising out of a settlement agreement, has had no influence on my decision that the

lease term requires lessees to account by the net real method. *Sun Oil Co. v. Govostes*, 474 F2d 1048, 1049 (2d Cir. 1973).

Until 1974, producers selling natural gas to SUG paid a base contract price plus a penny ($0.01) per thousand cubic feet (mcf) which it is claimed satisfied any obligation the producer had to account for liquids in the gas stream. From 1974 on, producers have received a BTU-adjusted price for gas sold to SUG. British Thermal Units (BTU's) are one way of measuring and valuing the liquid heating content of the natural gas stream. Whether it is the method which derives the highest royalties to the lessor depends on the BTU content and the base contract price of the gas. I have concluded that the Secretary was and is required to have producers account on behalf of the Tribe by a dual accounting method. Whether or not value is greater by the BTU-adjusted or the net real method, under the strict terms of the lease, does not relieve the Secretary of his duty to require producers to account both ways. And whether the "price plus a penny" method of payment made prior to 1974 satisfied the producers' obligation to account for liquids is a question which need not be reached in light of my conclusion that the Secretary was and is obliged to require dual accounting.

If it is without question, given the significantly higher prices received for gas in the San Juan Basin, that at present or, for example, since 1976, the BTU-adjusted method of accounting will always derive the highest royalty for the Tribe, the terms of the lease may be altered to relieve the Secretary, and thereby the producers, of accounting by both methods. I will not rewrite the terms of the lease for the parties. Provision for such alteration is made in the lease terms. Lease, *supra* at ¶ 3(g).

I concur with counsel for Exxon that the issue of dual accounting is "inextricably bound" to the issue of value.

Because the Secretary has erred in determining value without taking into account net realization, my summary judgment ruling on the issue of value, which otherwise would have been determinative on the dual accounting issue, must be withdrawn as incorrect as a matter of law.

It may be argued that I have taken and decided the dual accounting issue presently pending before the United States Interior Board of Land Appeals (IBLA). The issue before the administrative appellate body is whether Supron, a lessee and operator of the Lybrook plant during the time for which additional royalties were assessed (1974-6), was required to make a dual accounting because it was both a lessee and the operator of the Lybrook plant. The issue I have decided is whether, according to the terms of the lease, lessees (whether or not they are plant operators) are required to account by a dual accounting method. Evidence at trial revealed that the USGS certified this question to the Solicitor's Office of the Department of the Interior some time ago and has never received an answer. Whether the issue before the IBLA is subsumed in the issue I have decided is for it to determine. I would only comment that since Supron, like the other defendants, is a lessee, it, like the others, is obliged to account by the dual accounting method for the years in question. Of course, it need not reaccount for the years 1974-6 unless the Secretary concludes it has done so incorrectly.

Assuming *arguendo*, however, or should it be determined on appeal, that I have in fact invaded the province of the IBLA, I would support such action with the following observations. The dual accounting issue is a collateral issue necessary to the resolution of a primary issue pending before me now, i.e., whether the Secretary has breached his fiduciary duty to the Tribe. Plaintiff was not a party to the first appeal from the order of the oil and gas supervisor. Its motion to intervene in that proceeding was denied. Whether leave to intervene in the

second administrative appeal will be granted the Tribe is not apparent from the Record. Plaintiff, in this action, can and has litigated the issue of the Secretary's breach and necessarily thereby the issue of dual accounting. I see no reason to foreclose or postpone plaintiff's day in court on the basis of an administrative appeal in which plaintiff may or may not be permitted to participate.

Further, the act giving rise to Supron's administrative appeals was the December, 1976 letter order of the oil and gas supervisor. This order was promulgated more than a year and a half after plaintiff had filed suit in this Court seeking relief, *inter alia*, from defendants-lessees' alleged failure to account according to the lease terms. The action of the oil and gas supervisor came about at last in part as a result of the continual prodding of the Tribe and its attorneys, both before and after this action was filed. It is not readily apparent, even in the face of the substantial rule requiring deference to administrative proceedings, why the Tribe should be foreclosed from gaining resolution of an issue brought here as a result of belated agency action the administrative appeals from which have been and may continue to be without the Tribe's participation.

At trial, plaintiff's counsel stipulated that no claim was lodged against Southland for failing to account by the net real method, but that Southland's alleged failure to account for royalties on liquids prior to 1974 remained in issue. I hold, based on this stipulation, that neither the Secretary nor Southland need account by the net real method with regard to Southland's interests in the Tribe's leases for the years 1974 and thereafter. Acknowledging the inconsistency of this result, I state only that plaintiff is bound by the stipulation of counsel.

Whether the Secretary has breached his fiduciary duty by failing to comply with the terms of the lease in other particulars is an issue which need not be addressed here. The Secretary is directed to review the lease terms, the

regulations and the USGS Conservation Division Manual, Part 647, to consider whether further action is required to comply with his duty under the leases. Having found the Secretary to have breached his fiduciary duty to the Tribe in one respect, I can render, without more, declaratory judgment in favor of the Tribe to that effect. Granting such a declaratory judgment obligates the Secretary to require defendants-lessees, except Southland from 1974 forward and Supron from 1974-6, to render accounting by the dual accounting method for the years 1970 to the present. The cost of manufacturing allowance to be determined by the Secretary according to the terms of the lease and the regulations, 30 C.F.R. §§ 221.46, .51, shall be based on figures obtained from the Lybrook plant for the relevant years in question. The Secretary shall submit for my approval his accounting no later than ninety (90) days from the date of this Opinion. He shall incorporate into his own any accounting required of defendants-lessees for him to make his accounting complete and accurate.[13]

Because it is not certain that the Secretary's accounting will result in a ruling against defendant-lessees for additional royalties, it would be premature to rule on defendant Southland's cross-claim against Gas Company of New Mexico for payment of excess royalties under an indemnity provision in the gas purchase contracts effected between them. I will defer ruling on the claim of indemnity under the cross-claim pending receipt and approval of the Secretary's accounting.

Cancellation of the Leases

Included in the relief sought by plaintiff was a request that in the event it was determined that defendants-lessees have breached the terms of the leases the Secretary be ordered to cancel the leases on behalf of the

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[13] Such as corrected froms 9-361A.

Tribe. Although I have concluded that defendants-lessees have in fact breached the terms of the lease, I have stated that such breach was technical in nature by virtue of the Secretary's acquiescence in the manner by which defendants-lessees reported for accounting purposes and that the breach was through no apparent fault of defendants-lessees. Accordingly, I decline to require the Secretary to order the leases cancelled. Defendants have prevailed on the claims against them regarding offset wells and diligent development as well as those involving claims of antitrust violation. I see no reason to require defendants-lessees to give up the opportunity to continue working these leases for their own benefit as well as that of the Tribe.

I feel obliged to comment that the more appropriate remedy, were it available to the Tribe, would be the excision of the Secretary as the fiduciary through whom the Tribe is obliged to deal in its affairs with defendants-lessees. Plaintiff, like many Indian Tribes in recent times, has demonstrated its desire and ability to carry on business relations on its own, devoid of the paternalistic shroud in which it must be enveloped by the Secretary by virtue of the Tribe's legal status as a ward of the United States. It is Congress, however, and not the Court who is empowered to liberate the Indian Tribe from the protection imposed on them by the United States Government.

MOTIONS TO STRIKE

After the parties had filed post-trial briefs, defendant Supron moved to strike plaintiff's trial brief alleging several grounds as bases therefor. Defendant Southland joined in Supron's motion adopting Supron's grounds and stating an additional ground therefor. Defendant, Secretary of the Interior, also moved to strike certain portions of plaintiff's post-trial brief. Plaintiff responded to the motions. Having considered the motions and mem-

oranda of counsel and further being advised in the premises, I conclude that the motions to strike are not well taken and should be denied.

COSTS

Plaintiff, having prevailed on its common law claims in part shall recover costs thereon. Although I have concluded that the defendants-lessees have breached the terms of their leases, such breach was the result of the Secretary's own breach of his fiduciary duty to the Tribe. Accordingly, pursuant to 28 USC 2412, the Secretary shall bear a portion of plaintiff's cost insofar as such costs pertain to those issues on which plaintiff has prevailed against the Secretary.

Much of plaintiff's preparation was cumulative on its antitrust and common law claims. However, I find that the common law claims on which the plaintiff prevailed against the Secretary required more extensive and complex preparation than that required to present the antitrust claims. I conclude that two-thirds of plaintiff's costs should be assessed against the Secretary, the remainder to be borne by plaintiff. Defendants-lessees shall bear their own costs, as shall the Secretary.

An Order shall be entered in accordance with this Opinion.

/s/ E.L. Mechem
United States District Judge

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF NEW MEXICO

No. 75-247-M Civil

THE JICARILLA APACHE TRIBE,
Plaintiff,

v.

SUPRON ENERGY CORPORATION, *et al.*,
Defendants.

[Filed November 5, 1979]

ORDER

There having been a Memorandum Opinion filed which constitutes my Findings of Fact and Conclusions of Law, pursuant to Rule 52 of the Federal Rules of Civil Procedure; Now, Therefore,

IT IS ORDERED that plaintiff's antitrust claims be, and hereby are, dismissed with prejudice.

IT IS FURTHER ORDERED that plaintiff's claims against defendants Supron Energy Corporation, Southland Royalty Company and Exxon Company, U.S.A. (defendant energy companies), for failure to diligently develop the leases and for failure to protect the leased lands from drainage by drilling offset wells be, and hereby are, dismissed with prejudice.

IT IS FURTHER ORDERED that plaintiff's claim against defendant energy companies that they have breached the terms of the leases in that they have failed to account for and pay royalties according to the terms

of the leases be, and hereby is sustained. Any damages which may have accrued as a result of defendants' breach shall be determined after the Secretary's accounting, as required below, is made to and approved by me. Defendant energy companies shall make any accounting according to the terms of the leases which is required by the Secretary in order that his accounting to this Court be complete and accurate.

IT IS FURTHER ORDERED that declaratory judgment be entered to the effect that defendant Cecil Andrus, Secretary of the Interior, has breached his fiduciary duty to plaintiff by failing to insure diligent development of the leases, by failing to insure protection of the leased lands from drainage and by failing to account and to require defendant energy companies to account for and pay royalties according to the terms of the leases. The Secretary shall make an accounting based on the terms of the leases, the federal regulations pertaining thereto and the USGS Conservation Division Manual, Part 647, and any accounting by defendant energy companies required by the Secretary in order that his accounting be complete and accurate. The Secretary's accounting shall be made also in accordance with the findings and conclusions set out in the Memorandum Opinion on which this Order is based. The Secretary's accounting shall be made to me within ninety (90) days of the date of this Memorandum Opinion and Order.

IT IS FURTHER ORDERED that plaintiff's prayer that, based on defendant energy companies' breaches of the leases, the Secretary be ordered to cancel the leases which are the subject matter of this litigation be, and hereby is denied.

IT IS FURTHER ORDERED that ruling on defendant Southland's cross-claim against Gas Company of New Mexico be, and hereby is deferred pending receipt and approval of the Secretary's accounting.

IT IS FURTHER ORDERED that defendants' motions to strike all or part of plaintiff's post-trial briefs be, and hereby are, denied.

IT IS FURTHER ORDERED that two-thirds of plaintiff's costs be borne by the Secretary, that the remaining one-third be borne by plaintiff, and that all defendants bear their own costs.

/s/ E.L. Mechem
United States District Judge

APPENDIX G

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF NEW MEXICO

No. 75-247-M Civil

THE JICARILLA APACHE TRIBE,
Plaintiff,

v.

SUPRON ENERGY CORPORATION, *et al.*,
Defendants.

[Filed July 30, 1980]

MEMORANDUM OPINION AND ORDER

Pursuant to my Memorandum Opinion and Order of November 5, 1979 defendant Secretary of the Interior (Secretary) has presented for my review his accounting of royalites on oil and gas leases which are the subject matter of this litigation. Amendments to that accounting were presented on April 2, 1980. The defendant energy companies have filed their exceptions to the Secretary's accounting and a hearing on defendants' exceptions was held on May 13, 1980. At the conclusion of the May 13 hearing, counsel were directed to set out the issues agreed by them to be in dispute in addition to those raised by defendants' exceptions. The issues, as agreed on by counsel, were briefed [1] and this Opinion and Order follows.

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[1] Plaintiff's final Memorandum Brief on accounting issues was filed June 3, 1980 pursuant to an Order granting leave to do so.

Defendants' exceptions to the Secretary's accounting are substantially the same. Accounting figures were provided to the Secretary's representative, the USGS, by Supron for the interests it holds and for those held jointly by Exxon and Supron, which figures were adopted by Southland.[2] Accounting figures relating to the Lybrook plant were submitted to the USGS by Supron for the period January 1, 1970 to December 15, 1976. It is not clear, but it appears Supron also submitted plant data to USGS for the period December 16, 1976 to November 30, 1979. Sutherland Letter of March 5, 1980 attached to Secretary's Accounting. The method for dual accounting required by my November 5 Opinion and Order was set out in the January 1, 1980 letter of James Sutherland, Oil and Gas Supervisor for the Southern Rocky Mountain area. Supron Exhibit AA. A worksheet attached to that letter indicated the methodology by

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The contracts by which plaintiff's counsel has rendered services to the Tribe were disapproved on May 16 and 23, 1980 by the Area Director of the Albuquerque Area Office Bureau of Indian Affairs on the advice of the Field Solicitor. A Petition for Judicial Review of the actions of the Area Director is pending before the Hon. Santiago Campos, *Nordhaus, Haltom & Taylor, et al. v. Andrus, et al.*, Civ. 80-488-C (U.S.D.C.N.M., filed 6/13/80). The Tribal Council of the Jicarilla Apache Tribe, on June 20, 1980 rescinded its approval of counsel's contracts for services. The Tribe, through its President, has informed counsel that it wishes them to continue representing it in this matter. Counsel, at a hearing before me on June 26, 1980, informed me they cannot continue to represent the Tribe without a contract for services approved by the Tribe. At the hearing, counsel requested a stay of these proceedings pending resolution of the judicial review of administrative action now pending before Judge Campos, which request I have taken under advisement. Because the accounting issues resolved herein have been briefed fully by the parties, I have proceeded without feeling obliged to rule at this time on counsel's request for stay.

[2] Defendants, except for Supron with regard to the years during which it operated the Lybrook plant, have continued to restate their position that as non-plant operators they are not obliged to dual account for royalty purposes and do so only under Court order. Their continuing objection is duly noted.

which royalties would be computed on the BTU adjusted and the net realization methods, which together comprise dual accounting.

Defendants make no exceptions to the Secretary's accounting based on the BTU adjusted method. Their exceptions relate to the Secretary's calculation of royalties based on the net real method and also on the Secretary's use of a third accounting method, "minimum value," in the face of my ruling that dual accounting be required. Defendants claim that the Secretary's use of theoretical plant factors distorts the residue volume used in computing the value of residue gas produced at the tailgate of the Lybrook plant which, when computed with the value of liquids derived there, constitutes value for royalty purposes under the net real method of accounting. Defendants also complain of the Secretary's failure to allow a deduction for shrinkage of gas from the wellhead to the inlet of the Lybrook plant. The Secretary's method of calculating the cost of manufacturing allowance used in computing liquids values is attacked for its arbitrary allowance of only 10% for administrative costs and for its failure to deduct gas volumes used in processing other than between the inlet and the tailgate of the Lybrook plant.[3]

Issues raised by the parties in addition to the exceptions filed by defendant energy companies include the applicability of the New Mexico Natural Gas Price Act, as amended, N.M.S.A. §§ 62-7-1 through 10 (Supp. 1979) (NMNGPA or New Mexico Act), to gas production on the Jicarilla Reservation; the effect of the Natural Gas Policy Act of 1978, 15 U.S.C. §§ 3001 *et seq.* (NGPA or Act) on gas produced on the Jicarilla Reservation on or after January 1, 1978; whether defendants have

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[3] Defendants have also identified several clerical errors in the Secretary's accounting which have been corrected by his amendments to the accounting or will be amended, on counsel's representation, in the reaccounting to be made by the Secretary.

waived the inclusion of imputed interest as an allowable cost in the computation of the cost of manufacturing allowance for the Lybrook plant; and whether the cost of manufacturing allowance for the Lybrook plant should include the costs to the plant operator of fuel in excess of its wellhead price and of transporting gas from the wellhead to the plant inlet, costs excluded by the Secretary in his computation. These issues, set out in correspondence to me from the United States Attorney's Office, were substantially agreed on by counsel for defendants in subsequent correspondence in which they modified or rephrased issues while stating their basic agreement with the United States Attorney.

Defendant's exception to the Secretary's use of "minimum value" in addition to dual accounting in determining value for royalty purposes shall be overruled. The leases and the regulations require the Secretary to determine minimum value, taking sale price at the wellhead into account. Standard Lease Form 147, ¶ 3(c); 30 C.F.R. 221.47 (1979). Minimum value constitutes a floor price calculated on volumes at the wellhead and value as determined by the Secretary based on the mean price paid for gas in the field. Value, based on sale price, may exceed but may not be less than the Secretary's stated floor price. *Supron Energy Corp.*, 46 I.B.L.A. 181, 187-8 (1980). Minimum value is a limit on sale price, which price is the third "value" the Secretary must consider for royalty purposes. Defendants' argument that my Order requiring "dual accounting" limited the Secretary to using two, and no more, methods of determining value for royalty purposes takes the words "dual accounting" too literally. The Secretary must consider three methods of determining value for royalty purpose: 1) Sale price, taking minimum value into account; 2) BTU adjusted method; and 3) net real method. *Id.* Together the latter two comprise "dual accounting." Considered another way, the Secretary has used in fact only two means of

accounting, the first, sale price, taking into account minimum value, and the second, dual acounting.

As for the application of the NGPA to the Secretary's determination of value for royalty purposes, it is contract price, and not value, to which the restrictions of the NGPA apply. 15 U.S.C. §§ 3311 *et seq.* The NGPA places a ceiling price on the "first sale" of natural gas, 15 U.S.C. 3301(21)(A)(i), and therefore applies to the Secretary's determination of value insofar as it limits the price to be obtained for the first sale of natural gas. In this case the first sale occurs at the wellhead. Price at that point of sale is the starting point for the Secretary's determination of value for royalty purposes. Because the NGPA relates to price and not value, however, it may occur that the Secretary's determination of *value* exceeds the ceiling *price* set by the NGPA. There is no legal impediment to the Secretary's determining that value for royalty purposes exceeds sale price. This is not the first case in which value has been determined to be other than, and greater than, the contract price received for gas sold. *See, e.g., Mobil Oil Corp. v. FPC,* 463 F.2d 256, 364-5 (D.C. Cir.), *cert. den.,* 406 U.S. 976 (1972). "Escalating royalty costs" based on values in excess of sale price have been upheld as reasonable unless they force the producer into a net loss situation. *FERC v. Pennzoil Prod. Co.,* 439 U.S. 508 (1979). Because sale price is not binding on the Secretary in his determination of value for royalty purposes and because the NGPA applies to price, not value, the NGPA applies to the Secretary's determination of value only to the extent that he takes price into account, as he must, in making his determination of value for royalty purposes. 30 C.F.R. § 221.47 (1979). *See, Jicarilla Apache Tribe v. Supron Energy Corp.,* 479 F.Supp. 536 (D.N.M. 1979); *Supron Energy Corp.,* 46 I.B.L.A. at 188, 192; 25 C.F.R. 171.13; USGS Conservation Division Manual 647, 647.2.3; Lease, ¶ 3(c).

The NGPA by its own terms applies to the "first sale" of gas. The claim that it limits prices on residue gas produced at the tailgate of the Lybrook plant, therefore, is not persuasive. On the Jicarilla Reservation, gas is sold by producers at the wellhead, the point of "first sale." Subchapter I of the Act, 15 U.S.C. §§ 3311-33, is entitled "Wellhead Pricing." By definition, the NGPA does not apply to prices set on tailgate volumes of residue gas. Nor does the NGPA apply to the sale price of liquids at the tailgate. Its application is limited to sales of natural gas, 15 U.S.C. § 3301(1), and does not apply to liquid products.

The New Mexico Act establishes a ceiling for the price of natural gas produced in intrastate commerce. The NGPA expressly grants to the states power to prescribe lower ceiling prices on intrastate sales of natural gas than those imposed by the federal act. 15 U.S.C. 3432(a). The New Mexico Act does not apply to sales from the Jicarilla Reservation, however, in light of my ruling, the law of this case, that such sales constitute interstate commerce. 479 F.Supp. at 541. To the extent that defendants have reported lower prices received for natural gas produced from these leases on the assumption that the New Mexico Act applies, corrected figures shall be submitted to the Secretary for his reaccounting.

The Secretary, by counsel, has agreed to revise his accounting to reflect the proper pressure base for the years 1978 and '79 with regard to volumes at the Lybrook plant. Additionally, the Secretary's agreement to correct prices on Lease 104 for 1979 obviates the need for ruling on the admissibility of Supron's Exhibit 2 offered at the hearing on defendants' exceptions to the Secretary's accounting.

Defendants' exceptions to the Secretary's computation of cost of manufacturing allowances for the Lybrook plant will be sustained in part. The Secretary's claim that defendants have waived their claimed deduction for

imputed interest in the computation of the cost of manufacturing allowance used in determining liquid value in the net real method ought not stand based on the facts adduced at the May 13 hearing. The USGS employee who supervised the Secretary's accounting, Mr. Carmichael, testified that imputed interest which was not claimed was not allowed and that the imputed interest claimed for 1974 and '75 which was documented by defendants was permitted in the computation of cost of manufacturing allowances for those years. He admitted that not including the interest data made a significant change in the cost of manufacturing allowance computation. Mr. MacFaren, a Southern Union Company representative, testified that notice that imputed interest was a permissible deduction was forwarded to Southern Union Refining Company and not to Southern Union Company. He admitted that certain information was not submitted to the USGS because of time constraints imposed on the company by the agency. Exxon and Southland established that their reliance on Supron and Southern Union Company for figures submitted to the USGS precluded their knowing waiver of additional costs to be computed in the manufacturing allowance. Defendants' inadvertent omission of properly deductible costs does not constitute a knowing and voluntary waiver. I find that because USGS will have to prepare a reaccounting in any event and because no prejudice will follow them the inclusion of imputed interest figures properly deductible as a part of the cost of manufacturing allowance, such figures shall be supplied to the USGS and incorporated in its calculation of the cost of manufacturing allowance for net real accounting purposes.

Defendants also complained of the Secretary's utilization of a 10% figure for administrative costs in determining the cost of manufacturing allowance. The use of a 10% allowance, based on the USGS Conservation Division Manual, has been upheld by the Interior Board

of Land Appeals (IBLA) in its administrative review of the actions of the Oil and Gas Supervisor with regard to the leases at issue here. *Supron Energy Corp.*, 46 I.B.L.A. 181 (1980). The decision of the administrative agency is entitled to great weight and will not be disturbed unless it is shown to be arbitrary and capricious. Defendants claim that a 10% allowance is plainly incorrect in light of the cost to the plant operator of fuel substantially in excess of its wellhead price. Mr. Carmichael agreed that the actual cost of fuel to the plant operator was a deductible cost but refused to agree that the Lybrook plant operator was required to purchase gas to operate the plant instead of simply using gas from the stream and deducting it from tailgate volumes. I agree with Mr. Carmichael's unarticulated conclusion that the sale of gas to the plant operator at a price in excess of wellhead prices does not constitute an arms-length transaction which must be considered by the Secretary in computing the administrative cost properly allowed in computing the cost of manufacturing allowance.

Defendants also claim that the manufacturing allowance as computed by the Secretary was incorrect for failure to include a deduction for state and federal taxes. This issue has been resolved in the IBLA decision, 46 I.B.L.A. at 195, which decision shall not be disturbed as I find that it is reasonable and not arbitrary or capricious.

Defendants also complain that the refusal to permit a deduction for gas used between the wellhead and the inlet of the plant is incorrect. The decision of the IBLA, in light of my ruling below on the Secretary's net real accounting methodology, is the answer to defendants' claim.

> In fact, fuel costs and shrinkage are taken into account in the dual-accounting system. Royalty is determined on the basis of the volume of products *leaving* the processing plant. These volumes are clearly diminished when gas is lost in transit to the

> plant or is used in processing. That is, if gas is lost in transit and/or consumed during processing, the amount of royalty will be reduced accordingly because the amount of product sold at the tailgate of the plant will be reduced by an equivalent amount. Thus, the net-realization system automatically takes into account these factors. (emphasis in original) *Supron Energy Corp.*, 46 I.B.L.A. at 195-6.

On the basis of the decision of the IBLA and further because I agree with the conceptual analysis set out therein, defendants' exceptions regarding the Secretary's calculation of plant manufacturing allowance, except with regard to the deductions for imputed interest are overruled.

Defendants' remaining exceptions relate to the Secretary's methodology in calculating royalties on the net real accounting method. As stated above and in my November 5, 1979 Memorandum Opinion, 479 F.Supp. at 549, royalties are based on volumes and values. For purposes of the net realization method, the volumes used are the volumes of residue gas and liquids at the tailgate of the processing plant attributable *pro rata* to the volume of gas produced from each individual lease. Value at the tailgate for residue gas is the base price per MCF times a BTU adjustment on that gas.[4] Value for liquids is the net price per gallon of liquids produced.

Defendants' complaint with the Secretary's net real accounting addresses the Secretary's method of computing the volumes of residue gas and liquids produced at the tailgate attributable to each lease. Exhibit 8 to the Secretary's accounting sets out the method by which resi-

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[4] The BTU adjustment for residue gas is routinely lower than that for wellhead volumes because the extraction of liquids through drips and in the plant process results in the diminution of heating content and therefore BTU value for residue gas.

due volumes of gas and liquids allocable to each lease were derived.

> Residue volume allocated to the lease [is] calculated by multiplying the wellhead volume times the Plant Residue factor. The residue factor is calculated by dividing the total Plant Residue volume by the total inlet volume of gas at the plant.
>
> * * *
>
> The total number of gallons allocated to the lease owner [is] calculated by multiplying the wellhead volume times the Plant Liquid factor. The Plant Liquid factor is calculated by dividing the total gallons recovered at the plant by the total plant inlet volume. This factor represents the gallons recovered from each MCF of gas processed.

A mathematical configuration of the formula used by USGS to compute gas and liquids volumes at the tailgate allocable to each lease would appear as follows:

$$\frac{\text{Total Residue Gas Volume}}{\text{Total Inlet Volume}} \text{ X Wellhead Volume/Lease} = \text{Residue Gas Volume/Lease}$$

$$\frac{\text{Total Liquid Gallons}}{\text{Total Inlet Volume}} \text{ X Wellhead Volume/Lease} = \text{Liquid Gallons/Lease}$$

In each of these formulas, the "plant factor," for residue gas and liquids respectively, is represented by the first fraction set out above. Defendants energy companies claim that the "factor" to be multiplied by wellhead volumes per lease to determine residue gas volume and liquid gallons at the tailgate is more appropriately determined by replacing "total inlet volume" in the denominator of the first fractions in the above formulas with "total wellhead volume." This approach has recently been sustained in *Supron Energy Corp.*, 46 I.B.L.A. at 195-6, and is contemplated by 30 C.F.R. § 211.46. That regulation requires that the volumes of gas and liquids per lease on which royalties are to be computed

equal the volumes of those products respectively at the tailgate times the inlet gas allocable per lease, where inlet gas allocable per lease equals total inlet volume divided by total wellhead volume, divided by total inlet gas volume, all times wellhead volume per lease. Mathematically stated, these formulas appear as follows:

$$\frac{\text{Total Residue Gas Volume} \times \frac{\text{Total Inlet Volume}}{\text{Total Wellhead Volume}} \times \text{Wellhead Volume/Lease}}{\text{Total Inlet Volume}} = \text{Residue Gas Volume/Lease}$$

$$\frac{\text{Total Liquid gallons at Tailgate} \times \frac{\text{Total Inlet Volume}}{\text{Total Wellhead Volume}} \times \text{Wellhead Volume/Lease}}{\text{Total Inlet Volume}} = \text{Liquid Gallons/Lease}$$

Mathematical computation reveals that the formulas mandated in 30 C.F.R. § 221.46 are no different than those advocated by Supron and the other defendant energy companies.[5] The USGS' worksheet attached to Supron's Exhibit AA requires, when computing value for royalty purposes for residue gas, that the price be multiplied by the BTU adjustment factor and then by "residue volume," and for liquids, that the price per gallon be multiplied by "liquid gallons" and then by the quantity 1 minus the cost of manufacturing allowance. The cost of manufacturing allowance accounts for deductible costs between the inlet and tailgate of the plant. The formula set out in § 221.46, and implemented by USGS in its own worksheet accounts for reasonably deductible costs between the wellhead and the inlet. Together they contemplate the entire process.

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[5] "Total inlet volume," in both the numerator and denominator of the first fraction in these formulas, cancels out, leaving precisely the formulas advocated by defendant energy companies.

The IBLA correctly interpreted the use of the latter formulas above to make allowance for the shrinkage claimed by the defendants herein. 46 I.B.L.A. at 195. Indeed, defendants have agreed that if their proposed formula is adopted by the Court for use in the Secretary's reaccounting, such computation appropriately accounts for their claimed deduction for gas lost in transit and used in processing other than between the inlet and the tailgate of the Lybrook plant. The Secretary claims that if the formula suggested by defendants is adopted, they will derive a double benefit with regard to gas which is either separated out or used for processing between the wellhead and inlet of the plant. No claim is made that royalties are not paid on the drip volumes separated out between the wellhead and the inlet. Gas not separated by drips is either used in the processing scheme or "unavoidably lost." I find the former to be a deductible volume, 30 C.F.R. § 211.46, and the Secretary agrees the latter is a deductible volume.

The theoretical residue factor derived by USGS by placing total inlet volume instead of total wellhead volume in the denominator of the first fraction of its mathematical formulas by which it computed residue gas volumed and gallons of liquid at the tailgate is incorrect. Nor does it comport with its own worksheet formula. The Secretary has offered no substantial justification for using theoretical rather than actual residue volumes in computing royalties. The Secretary shall reaccount such volumes using the appropriate formulas set out above.

Although I have relied on the decision of the IBLA in *Supron Energy Corp.*, 46 I.B.L.A. 181 (1980), this opinion is not to be construed as constituting judicial review thereof. No request has been made for such review at this time. My reliance on the IBLA decision is based on its unique applicability to the facts of this case and on what I find to be its correct analysis of issues to be determined here.

The Secretary, through his representative, shall present to me this reaccounting based on counsel's agreements concerning the various clerical errors discovered in the Secretary's initial accounting and on my rulings herein. Such accounting shall be presented for my consideration no later than 30 days from the date of this Memorandum Opinion and Order. The parties shall have ten days from the date they receive the Secretary's reaccounting to file their exceptions thereto. Having ruled once on the parties' exceptions, I anticipate no further exceptions except with regard to clerical errors. Additional figures, if any, required by the Secretary to make his reaccounting shall be provided by defendants if necessary.

Defendants Exxon and Gas Company of New Mexico have requested a ruling at this time on the "excess royalty" provisions in their purchasing agreements with regard to additional royalties which may result from the Secretary's reaccounting. Those issues are the substance of cross-claims lodged by Southland and Exxon against Gas Company of New Mexico and need not be resolved at this time. Ruling on the cross-claims, therefore, will be deferred pending receipt and approval of the Secretary's reaccounting.

IT IS SO ORDERED.

/s/ E.L. Mechem
United States District Judge

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF NEW MEXICO

No. 75-247-M Civil

JICARILLA APACHE TRIBE,
Plaintiff,

v.

SUPRON ENERGY CORP., *et al.*,
Defendants.

[Filed Jan. 26, 1981]

ORDER

This matter comes up for consideration on the motions to reconsider filed by the Jicarilla Apache Tribe (Tribe), the Secretary of Interior (Secretary), Gas Company of New Mexico (GCNM), Exxon Company, U.S.A. (Exxon), and Southland Royalty Company (Southland) and the motion of Southern Union Production Company (Supron) to clarify my Memorandum Opinion and Order of July 30, 1980. To be considered also are Southland's and Exxon's motions requesting leave to file amended crossclaims against GCNM and the motions of the Secretary, Southland, Supron and GCNM to strike the deposition of Dr. Alfred L. Parker. Finally, the Secretary has filed his amended accounting for approval.

Issues raised by the motions for reconsideration and clarification are: (1) whether my findings that the gas produced on the Jicarilla Apache Reservation is in in-

terstate commerce and therefore not subject to regulation by the New Mexico Natural Gas Price Act as amended, N.M. Stat. Ann. §§ 62-7-1 through 10 (Supp. 1979) (New Mexico Act) is in error; (2) whether New Mexico is precluded from asserting regulatory jurisdiction over gas produced on the Jicarilla Apache Reservation by the Indian Commerce Clause of the United States Constitution. U.S. Const. Art. 1, § 8; (3) whether state regulation of the price to be charged for gas produced on the Jicarilla Apache Reservation has been preempted by federal statutes and regulations; (4) whether value for purposes of royalty computation may exceed the maximum price of the gas as established by the applicable regulatory act; (5) whether the net real method of accounting based on tailgate volumes requires the Secretary to determine royalties due on gas used and drip gas collected between the wellhead and the inlet of the processing plant.

Interstate Commerce

My finding that the actions forming the basis of the Tribe's antitrust claims have an effect on interstate commerce does not necessitate the conclusion that the gas produced on the Jicarilla Apache Reservation is not subject to regulation by the New Mexico Gas Price Act. Subject matter jurisdiction over antitrust claims resides in Federal District Court on a finding that the activities which form the basis for the alleged antitrust violations are in or effect interstate commerce. *Hosp. Bld. Co. v. Trustees of Rex Hosp.*, 425 U.S. 738 (1976). The Natural Gas Policy Act of 1978, 15 U.S.C. §§ 3301 through 3432 (1976) (NGPA) allows a state to set the maximum price for gas below the maximum established by the NGPA "for the first sale of natural gas produced in such state." 15 U.S.C. 3432(a). The gas which is the subject matter of this litigation is produced and sold in New Mexico. Although the production and sale of Jicarilla gas does have an effect on interstate commerce

for purposes of subject matter jurisdiction over antitrust claims, the gas is nonetheless produced and sold in New Mexico. My previous finding that the Jicarilla gas is not subject to state regulation because of the interstate character of that gas was in error.[1] The Secretary need not revise his accounting on this issue, however, in light of my conclusion, *infra*, that the New Mexico Legislature did not intend the New Mexico Act apply to the first sale of natural gas produced on the Jicarilla Apache Reservation.

Preemption

Plaintiff argues that 30 C.F.R., Part 221 and 25 C.F.R. Part 171, have preempted state regulation of the price to be charged for gas produced on the Jicarilla Apache Reservation. Although the regulations relate to mineral development on an Indian reservation, they do not set the price which may be charged for natural gas produced on an Indian reservation. The NGPA controls the price for regulated gas with the exception which allows a state to set a lesser maximum price for intrastate gas. The price of regulated gas produced on the Jicarilla Apache Reservation is either controlled by the NGPA or the state act passed pursuant to the exception in the NGPA. Federal regulations which control aspects of mineral production from Indian lands other than the price which may be charged for natural gas have not preempted state regulation of the price to be charged for Jicarilla gas.

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[1] The Tribe argues the New Mexico Act cannot regulate the price of Jicarilla gas because the Tribe may want to take royalty gas in kind and sell that gas in interstate commerce. The Tribe has not yet, however, taken any royalty in kind nor has the Tribe sold any natural gas in interstate commerce. I need not consider speculations on the Tribe's intentions in order to determine whether the gas produced on the Jicarilla Reservation is beyond the regulatory power of the New Mexico Act.

Indian Commerce

Plaintiff's argument that the New Mexico Act may not control the price of natural gas produced on the Jicarilla Apache Reservation because such control would be inconsistent with the Indian Commerce Clause presents a constitutional question which I need not reach. Well-settled rules of statutory construction require I not reach the constitutional question in the absence of a "compelling necessity" to do so. *Uhl v. Ness City, Kansas*, 590 F.2d 839, 841 (10th Cir. 1979). Furthermore, considerations of comity and respect for state legislative judgment require I find the New Mexico Act constitutional if the act reasonably may be interpreted so as not to conflict with the federal Constitution. *Swan v. Charlotte-Mecklenburg Bd. of Ed.*, 312 F.Supp. 503 (W.D.N.C. 1970) aff'd, *North Carolina State Bd. of Ed. v. Swan*, 402 U.S. 43 (1971).

New Mexico has disclaimed all right and title to Indian lands. N.M.Const. art. 21, § 2.[2] Although this type of disclaimer has not been interpreted literally, it has been recognized to preclude state jurisdiction over Indian lands, absent express Congressional authorization, where a state's attempt to assert jurisdiction would interfere with a tribe's right to make its own laws and be governed by them. *Mescalero Apache Tribe v. Jones*, 411 U.S. 145 (1973) citing *Williams v. Lee*, 358 U.S. 217 (1959).

I find that New Mexico did not attempt to assert jurisdiction over Jicarilla land when the New Mexico Act was enacted.

New Mexico tax statutes regarding oil and gas production allow taxes to be collected from Indian lands "to the extent authorized or permitted by law." *See* N.M. Stat. Ann. §§ 7-29-4; 7-31-4; 7-30-4 (1978). Those stat-

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[2] A corresponding provision appears in the Enabling Act for New Mexico, 36 Stat. 557, Act of June 10, 1910.

utes illustrate that the New Mexico Legislature is aware that the State may assert jurisdiction over Indian land if there is no infringement upon a tribe's right to govern itself or if Congress has expressly given its consent to the State to assert that jurisdiction. Additionally, in determining legislative intent, "It is always appropriate to assume that our elected representatives, like other citizens know the law . . . ." *Cannon v. University of Chicago*, 441 U.S. 677, 696 (1979). I conclude the New Mexico legislature was aware of the limits upon its power to regulate Indian affairs when it enacted the New Mexico Natural Gas Price Act. Because of the New Mexico Legislature's awareness of the limits upon its authority to act on Indian lands and its failure to make the New Mexico Act specifically applicable to gas production from Indian lands, I conclude the New Mexico Legislature did not intend the New Mexico Act to control the price for the first sale of gas produced from Indian lands.

Even if the New Mexico Act specifically included gas produced from Indian lands, the State's attempt to regulate the price of that gas would be a clear violation of the Tribe's right to make their own laws and be governed by them.[3]

The Tenth Circuit recently held that the Jicarilla Apache Tribe has a retained sovereign right to levy severance taxes upon oil and gas production on their

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[3] Infringement upon the Tribe's right to make their own laws and be governed by them is the appropriate constitutional standard because there is no congressional authorization allowing New Mexico to set the price of Jicarilla gas. It is well settled that a federal statute granting jurisdiction to a state over Indian affairs must do so expressly. *McClanahan v. Arizona Tax Comm.*, 411 U.S. 164 (1973). The NGPA does not expressly grant power to New Mexico to set the maximum price of gas produced from Indian lands. Therefore, the proviso in the NGPA allowing state regulation of intrastate gas could not be a signal to the New Mexico Legislature that it was free to regulate the price of that gas.

reservation.[4] *Merrion v. Jicarilla Apache Tribe*, 617 F.2d 537 (10th Cir. 1980), *cert. granted* 48 L.W. 2605 (1980) No. 80-11. The Tribe has a similar right to receive royalty for gas produced from their Reservation based upon a price at or below the federal maximum established in the NGPA. The Tribe's interest in income generated from oil and gas production on its reservation is obvious. Because the price received for gas is one variable which the Secretary must consider in determining value for royalty purposes, the royalty income the Tribe receives for its gas will be affected by the price charged for that gas. Additionally, the Court in *Merrion*, noted that 25 U.S.C. § 398(c) (1976) granting to the states power to levy severance taxes on oil and gas production from Executive Order Reservations was an integral element of the Act of March 3, 1927, granting to the Indians all the royalty, bonus and rental from oil and gas leases on their reservations. 25 U.S.C. § 398(b) (1976). The Court further noted that the majority of legislators voting for those statutes "obviously thought that all benefits from the minerals on the reservation belong to the Indians." *Id.* at 547.

This observation and the holding in *Merrion* strongly support the conclusion that the right to receive royalty based upon a price at or below the federal maximum is an incident of tribal sovereignty. Reduced revenues resulting from State control of the price to be charged for Jicarilla gas, had the New Mexico Act attempted to assert that jurisdiction, would be an infringement upon the Tribe's right to make their own laws and be governed by them.

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[4] The State of New Mexico may also levy taxes upon gas severed from the Jicarilla Apache Reservation pursuant to the express authorization to do so found at 25 U.S.C. § 398(c). The right of the state to levy this tax, however, is not inconsistent with the Tribe's inherent right as sovereign to levy a similar tax. *Merrion, Id.* at 547.

Value

I decline to disturb my ruling that value for royalty computation purpose may exceed the maximum price of the gas as established by the NGPA. This issue was extensively briefed before my November 5, 1979 finding relating to value and I am not persuaded that that finding was in error.

Net Real Accounting

The Secretary and the Tribe argue the net real method of accounting requires the Secretary to compute royalties on gas used between the wellhead and the inlet of the processing plant rather than solely on volumes of liquids and residue gas at the outlet of the processing plant. The Secretary also argues royalty must be computed upon liquid hydrocarbons collected as drip gas in the collection system in addition to volumes of liquids and gas at the outlet of the processing plant. A distinction must be drawn between drip gas collected and gas used to compress or otherwise condition the gas.

As noted in my Opinion and Order of November 5, 1979, the net real method of accounting contemplates royalty computed on the aggregate value of products produced from the leases whether the products are recovered at the outlet of the processing plant or recovered as drip gas in the collection system. 479 F.Supp. at 550 n.12. Because drip gas is collected and sold and is not unavoidably lost or used in processing, the Secretary must account for volumes of liquids collected as drip gas in addition to the products leaving the outlet of the processing plant under the Net Real Method of Accounting.

The Secretary shall have 30 days from the date this Opinion is filed to supplement his reaccounting to include liquids collected as drip gas. GCNM shall provide the Secretary with the information necessary to supplement his reaccounting. The amount of liquids collected as drip gas which originate from the Jicarilla Leases shall be calculated in a manner similar to the calculation of the Residue Factor and the Liquid Factor contained in Ex-

hibit 12 of the Secretary's reaccounting. Drip factor shall, therefore, be calculated in the following manner:

$$\text{Drip Factor} = \frac{\dfrac{\text{Drip Volume X Tot. Jic. Wellhead Vol.}}{\text{Tot. Wellhead Vol.}}}{\text{Tot. Jic. Wellhead Vol.}}$$

The Secretary shall then determine drip liquid gallons on a lease-by-lease basis by multiplying the various wellhead volumes by the drip factor. Drip liquid gallons multiplied by the applicable drip liquid price less the manufacturing allowance provides drip liquid value. The drip liquid value attributed to the Jicarilla Leases shall then be combined with other Total Value data contained in Exhibits 4, 5, 6 and 7 of the Secretary's reaccounting to determine aggregate value utilizing the Net Real Method of Accounting.

The Secretary's and the Tribe's arguments that royalty must be computed on gas used to compress or otherwise condition the gas between the wellhead and the inlet of the processing plant are without merit. Although the federal defendant admits computation based upon outlet volumes is the procedure contemplated by 36 C.F.R. 221.46, he argues nonetheless that he must be allowed to exercise his discretion to utilize a different method to fully protect the Tribe's royalty interest pursuant to 30 C.F.R. 221.46(e). That Section allows the Secretary to employ a method other than the method contemplated by the regulation if the latter method is not "practicable". There was no showing that computation of royalties based upon outlet volumes is not practicable. With the exception of data relating to drip gas collected, which will be supplied to the Secretary pursuant to this Order, all of the data necessary to utilize the accounting method contemplated by 30 C.F.R. 221.46 has been furnished by the producers. The Secretary need not include in his net real accounting gas used to compress or otherwise condition the gas between the wellhead and the inlet of the processing plant.

Parker Deposition

I decline to grant defendants' motions to strike the deposition of Dr. Alfred L. Parker.

Exxon's and Southland's Crossclaims

Exxon's and Southland's motions requesting leave to file amended crossclaims against GCNM shall be denied. The crossclaims which Exxon and Southland seek to amend request from GCNM reimbursement for any "excess royalty" which the producers are required to pay the tribe as a result of the Secretary's reaccounting. The amended crossclaims request not only "excess royalty" as that term is defined in the contract between the producers and GCNM but also the difference between the amount GCNM paid the producers on the assumption the New Mexico Act controlled the price of the gas and the contract price which is greater than the price allowed by the New Mexico Act.

Although I have concluded that the New Mexico Legislature did not intend the New Mexico Act have application on the Jicarilla Reservation, I similarly conclude the producers' amended crossclaims would inject new issues into this lawsuit which would unduly complicate this case and which would better be brought separately.

Because Southland and Exxon are not the only producers from whom GCNM purchases gas produced on Indian lands, it may be necessary for GCNM to join other producers in order to avoid inconsistent judgments respecting GCNM liability to those producers. Such joinder would unduly complicate this litigation and delay final resolution of plaintiff's claims. Additionally, since Southland and Exxon are free to file suit against GCNM, they will suffer no prejudice by the denial of their motions. Supron, Exxon, and Southland shall submit pleadings documenting the amounts they request in

their respective crossclaims within 20 days of the filing of the Secretary's supplemented reaccounting. The parties may also submit additional argument on the validity of those crossclaims within the same time limitation. Partial Final Judgment will be entered upon receipt of the Secretary's supplemented reaccounting. Now, Therefore,

IT IS ORDERED that Supron's motion to clarify and the motions to reconsider filed by GCNM, Southland and Exxon, insofar as those motions relate to the applicability of the New Mexico Gas Price Act to gas produced on the Jicarilla Apache Reservation, shall be, and hereby are, denied.

IT IS FURTHER ORDERED that the motions to reconsider filed by Southland and Exxon arguing that value may not exceed the maximum price of gas established by the NGPA shall be, and hereby are, denied.

IT IS FURTHER ORDERED that the motions to reconsider filed by the Secretary and the Tribe insofar as those motions argue that royalties should be computed on gas used between the wellhead and the inlet of the processing plant shall be, and hereby are, denied.

IT IS FURTHER ORDERED that the Tribe's motion to reconsider insofar as that motion argues that royalty must be computed on the value of drip gas collected in the gas collection system shall be, and hereby is, granted. The Secretary shall compute the value of those liquids using the information supplied by GCNM and supplement his accounting accordingly. The Secretary shall submit his supplemented reaccounting within thirty days from the date this order is filed.

IT IS FURTHER ORDERED that the motions of Southland and Exxon requesting leave to file amended crossclaims shall be and hereby are, denied. Supron,

Southland and Exxon shall submit pleadings specifying the amounts requested in their pending crossclaims within twenty days from the date the Secretary's supplemented reaccounting is filed.

/s/ E.L. Mechem
United States District Judge

APPENDIX H

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF NEW MEXICO

No. 75-247-M Civil

JICARILLA APACHE TRIBE,
Plaintiff,

v.

SUPRON ENERGY CORPORATION, *et al.*,
Defendants.

[Filed June 1, 1981]

MEMORANDUM OPINION

This case was tried without a jury in May and June of 1979. By my Memorandum Opinion and Order of November 5, 1979, I determined that the defendant energy companies had breached the terms of their leases with the Jicarilla Apache Tribe by failing to account for and pay royalties to the Tribe according to the terms of the leases and the federal regulations which inform them. I also granted declaratory judgment in favor of the Tribe that the Secretary of Interior had breached his fiduciary duty to the Tribe by failing to account and to require the defendants to account for and pay royalties using a dual accounting method.

On March 17, 1980, the Secretary filed his accounting of royalty due the Tribe. A hearing was held on defendants' exceptions to the Secretary's accounting on May 13,

1980. I sustained several of defendants' objections and the Secretary was ordered on July 30, 1980, to submit a reaccounting of royalty due. That accounting was filed on September 10, 1980. Again, I considered objections to the Secretary's Reaccounting and I ordered the Secretary, on January 27, 1981, to supplement his reaccounting to include royalty due the Tribe on "drip gas" recovered in the gas collection system. The Secretary's supplemental reaccounting was filed for my approval on March 23, 1981. I find that the Secretary's supplemental reaccounting correctly computes the additional royalty due the Tribe as required by my orders of November 5, 1979, July 30, 1980 and January 27, 1981. The Secretary's supplemental reaccounting will therefore be approved.

The Jicarilla Apache Tribe shall recover $24,144.50 from Southland Royalty Company to compensate it for royalty due on production from Southland's leases with the Tribe from 1970 to 1974. The Tribe shall also recover $262,087.24 from Supron Energy Corporation to compensate the Tribe for royalty due on production from Supron's leases with the Tribe from 1970 to 1973 and from 1977 to November 30, 1979. Exxon Company, U.S.A., shall pay the Tribe $57,705.07 to compensate it for royalty due on production from Exxon's leases with the Tribe from 1970 to November 30, 1979.

In my Memorandum Opinion and Order of November 5, 1979, I deferred ruling on defendant/producer's crossclaims against Gas Company of New Mexico until the Secretary's accounting was approved and it was determined whether or not producers would owe additional royalty to the Tribe. It is now appropriate to rule on those crossclaims.

Southland's Crossclaim

Southland seeks reimbursement from Gas Company of New Mexico for the additional royalty which I have determined Southland must pay the Tribe because of my

order requiring dual accounting from 1970 to 1974 and 1979 forward. Southland sold natural gas which was produced from the Jicarilla Apache Reservation to Gas Company under gas purchase contracts dated December 12, 1953 and June 28, 1976. Both contracts contain provisions which require Gas Company to compensate Southland for "excess royalty". Southland's claim for excess royalty from 1970 to 1974 is based upon the excess royalty clause in the 1953 gas purchase contract. That clause provides:

> Buyer agrees to reimburse seller for all excess royalty which seller shall be required to pay to the United States Government on the gas, gasoline and other products delivered to and taken by buyer pursuant to this agreement.
>
> Excess royalty payments shall mean the amount by which the actual royalties required to be paid shall exceed what would have been paid if the royalty had been computed upon the mcf prices received by seller from buyer under this agreement . . . .

Gas Company argues that it is not required to compensate Southland for excess royalty under the 1953 gas purchase contract because royalty payments are made to the Tribe rather than to "the United States Government" and the excess royalty clause is, therefore, not applicable. Although the Tribe is the ultimate beneficiary of the royalty received, 25 U.S.C. §§ 398(a) through (3) and 25 C.F.R. 171.12 (1980) require that royalty payments be tendered to the United States. Paragraph 3(c) of the leases between the Tribe and Southland requires royalty payments be made to the U.S.G.S. for the benefit of the Tribe. Royalty payments have been at all relative times tendered to the United States. Although the royalty payments are currently made by check payable to the Tribe, the checks were initially payable to the Treasurer of the United States. Such payments are payments "required to be paid to the United States" and the

excess royalty provision in the 1953 gas purchase contract between Southland and Gas Company requires Gas Company to reimburse Southland for those payments. Southland shall recover $24,144.50 from Gas Company to compensate it for excess royalty Southland must pay the Tribe for gas production from 1970 to 1974.

Southland also seeks recovery for excess royalty payments made to the Tribe for gas produced from December 1979 to December 1980 under the terms of the June 28, 1976 gas sales contract between Southland and Gas Company. That contract provides for reimbursement by Gas Company for excess royalty required to be paid "to any party." Gas Company argues that royalty payments for production from December 1979 to December 1980 were not required to be paid because Southland was relieved of its obligation to account for royalty utilizing the dual accounting method by virtue of a stipulation entered into at trial by counsel for Southland and the Tribe. Counsel stipulated that no claim was lodged against Southland for its failure to account by the net real method from 1974 forward. Gas Company argues that this stipulation relieves Southland of its obligation of dual accounting not just for past production to the date of trial, but also of any obligation to account for royalty utilizing dual accounting indefinitely.

My order of November 5, 1979 required the Secretary to account for royalty due on Southland's leases with the Tribe on past production other than from 1974 to the date of trial. That order similarly required the Secretary to utilize dual accounting prospectively for royalty due the Tribe under its leases with Southland. Counsel for Southland and the Tribe, the parties who entered into the stipulation, maintain the stipulation only referred to past production and they have interpreted my order accordingly. Counsel's stipulation that the Tribe lodged no claim for dual accounting against Southland

from 1974 to the date of trial, does not relieve Southland of its obligation to account for royalty utilizing dual accounting for production occurring after the stipulation. Southland shall recover from Gas Company $73,208.17 to compensate it for excess royalty for gas production from December 1979 to December 1980.

An order of the U.S.G.S. dated December 9, 1976, required Southland to pay to the Tribe $104,764.28 additional royalty for the years 1971 through 1973. Southland appealed that order and the appeal is presently pending before the Honorable Santiago Campos in this Court as No. 80-261-C. Gas Company reimbursed Southland for this royalty assessment although Gas Company and Southland stipulated the payment was not an admission that Gas Company was responsible for such excess royalty. Southland requests I include the $104,764.28 in its recovery against Gas Company on its crossclaim in this action subject to credit in favor of Gas Company for the $104,764.28 which Gas Company paid to Southland. Although I note Southland's request, I conclude that it is not appropriate to include the sum assessed by the U.S.G.S. in the award to Southland in its crossclaim in this action in light of the appeal now pending before Judge Campos.

Southland's crossclaim also requests I order Gas Company to render all future accountings of the royalty due the Tribe from Southland's wells. Southland maintains that Gas Company has possession of much of the production information necessary to account for royalty due the Tribe and that Gas Company should therefore be required to render such accountings. The leases between Southland and the Tribe require Southland to account for royalty due the Tribe. Gas Company agreed in its stipulation for settlement with the plaintiff to furnish information necessary to properly account for royalty due the Tribe. Southland's request that I order Gas Com-

pany to account for royalty due on production from Southland's leases with the Tribe shall be denied.

Supron's Crossclaims

Supron's crossclaim against Gas Company of New Mexico for excess royalty on production before August 20, 1976 is based upon a clause in the 1961 gas purchase contract entered into by Supron and Gas Company. That clause requires Gas Company to pay Supron a price equivalent to any higher price paid by Gas Company to Southland. Supron argues that if Southland recovers any excess royalty under the excess royalty clause in its gas purchase contract with Gas Company, the price equalization clause in the Supron gas purchase contract requires that Supron receive a similar adjustment. The price equalization clause contains an exclusion which provides

> In determining whether any higher price is being paid by a buyer for purposes of this article VIII . . . there shall be disregarded any excess or premium amounts paid or required to be paid on account of gas royalty or overriding royalty or on account of liquifiable hydrocarbon content specifically recognized.

Supron argues the language "on account of liquifiable hydrocarbon content specifically recognized" was intended to exclude from the price equalization clause royalty paid by other producers for btu content in the gas stream prior to processing. Supron argues further that the royalty it is required to pay the Tribe utilizing net realization accounting does not compensate the Tribe for "liquifiable hydrocarbon content specifically recognized", but rather the payments compensate the Tribe for liquids actually extracted and sold at the outlet of the Lybrook plant and the exclusion is, therefor, inapplicable. I find Supron's argument unavailing.

The price equalization clause is unambiguous. It excludes consideration of royalty paid on account of gas or on account of liquid hydrocarbon. The btu method of adjustment and net realization accounting, which together comprise dual accounting, insure the Tribe receives royalty on the gas and liquids in the gas stream. Such royalty payments may not be considered in determining whether Southland received a higher price than Supron for equivalent gas under the price equalization clause in the 1961 gas purchase contract. Supron's claim against Gas Company for royalty due the Tribe from 1970 to 1971 shall be denied.

Supron also claims compensation for royalty which it is required to pay the Tribe for production from 1977 to 1979 utilizing dual accounting under the excess royalty clause in its gas purchase contract with Gas Company as amended on August 20, 1976. The amended contract required Gas Company to reimburse Supron for

> the amounts which seller may be required to pay any party as royalty on such gas, extracted by-products or other products in excess of the royalty paid or payable to such party based on the price actually received by seller for sales of such gas, extracted by-products or other products.

Other than asserting general objections to my earlier orders in this case, Gas Company did not object to Supron's request for excess royalty for production from 1977 to 1979. Supron shall recover $232,528.23 to compensate it for excess royalty required to be paid the Tribe for production from 1977 to November 30, 1979.

Exxon's Crossclaim

Exxon requests reimbursement for excess royalty which it is required to pay the Tribe for production from 1977 to November 30, 1979 pursuant to the excess royalty clauses in its gas purchase contracts with Gas Com-

pany dated March 26, 1976 and April 14, 1978. Again, other than asserting its disagreement with the earlier orders in this case upon which the Secretary's accounting is based, Gas Company did not object to Exxon's request for compensation for excess royalty payments. Exxon shall recover $28,817.94 from Gas Company pursuant to the excess royalty provisions in the gas purchase contracts to compensate it for royalty which Exxon is required to pay the Tribe for production from 1977 to November 30, 1979.

/s/ E.L. Mechem
United States District Judge

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF NEW MEXICO

No. 75-247-M Civil

JICARILLA APACHE TRIBE,
Plaintiff,

v.

SUPRON ENERGY CORPORATION, *et al.*,
Defendants.

[Filed June 1, 1981]

ORDER

The Memorandum Opinion having been entered in this matter deciding all of the issues remaining; Now, Therefore,

IT IS ORDERED that the Secretary of Interior's supplemental reaccounting filed with this court on March 23, 1981, shall be, and hereby is, approved.

IT IS FURTHER ORDERED that the Jicarilla Apache Tribe shall be, and hereby is, awarded $24,144,50 from Southland Royalty Company.

IT IS FURTHER ORDERED that the Jicarilla Apache Tribe shall be, and hereby is, awarded $262,087.24 from Supron Energy Corporation.

IT IS FURTHER ORDERED that the Jicarilla Apache Tribe shall be, and hereby is, awarded $57,705.07 from Exxon Company, U.S.A.

IT IS FURTHER ORDERED that Southland Royalty Company shall be, and hereby is, awarded $97,352.67 from Gas Company of New Mexico.

IT IS FURTHER ORDERED that Supron Energy Company shall be, and hereby is, awarded $232,528.23 from Gas Company of New Mexico.

IT IS FURTHER ORDERED that Exxon Company, U.S.A. shall be, and hereby is, awarded $28,817.94 from Gas Company of New Mexico.

/s/ E.L. Mechem
United States District Judge

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF NEW MEXICO

No. 75-247-M Civil

JICARILLA APACHE TRIBE,
Plaintiff,

v.

SUPRON ENERGY CORPORATION, *et al.*,
Defendants.

[Filed July 1, 1981]

ORDER

This matter comes up for consideration on the Court's own motion pursuant to Rule 60(a) of the Federal Rules of Civil Procedure. It appearing that there is an error in the order filed in this matter on June 1, 1981, and that the same should be corrected. Now, Therefore,

IT IS ORDERED that the award made to the Jicarilla Apache Tribe from Exxon Company, U.S.A. at line 13 of the Order of June 1, 1981, shall be, and hereby is, amended to award the Tribe $57,705.07 rather than $57,507.07.

/s/ E. L. Mechem
United States District Judge

APPENDIX I

UNITED STATES DEPARTMENT
OF THE INTERIOR
OFFICE OF HEARINGS AND APPEALS
INTERIOR BOARD OF LAND APPEALS
4015 Wilson Boulevard
Arlington, Virginia 22203

SUPRON ENERGY CORP. *ET AL.*

IBLA 79-374, etc. Decided March 21, 1980

Consolidated appeals from decisions of the Acting Deputy Commissioner, Indian Affairs, IND-9, 10, 13, 14, 15, and 16-O&G, affirming decisions of the Geological Survey's Area Oil and Gas Supervisor, Albuquerque, New Mexico, establishing values for determining royalty on Jicarilla Apache tribal oil and gas leases and requiring initiation of a dual accounting system.

Affirmed in part; remanded in part for further documentation.

1. GEOLOGIC SURVEY; INDIAN LANDS—Tribal Lands; REGULATIONS—Applicability—Interpretation; ROYALTIES—Base Value—Computation.

   A Geological Survey Area Supervisor is acting within the authority granted to him by applicable provisions of Indian oil and gas leases and Indian and Federal royalty regulations when he decides to adopt the greater of either 1) actual sales prices of production from the leased lands or 2) a substitute price computed by him which is reasonable based on sales prices from all production from other similar tribal leases in the area, as the "value" of gas

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For Index Code see:

46 IBLA 197

produced on these leases, and when he directs lessees to compute royalty based on the greater of the two values so calculated.

2. GEOLOGIC SURVEY; INDIAN LANDS—Tribal Lands; REGULATIONS—Interpretation; ROYALTIES—Base Value—Computation.

   Where the Area Supervisor assembles data concerning sales from all Jicarilla tribal leases for a particular year and determines the medial sales price, his use of this figure as a minimum floor price by which to determine value will be affirmed, as this decision is within the latitude afforded him, and this price is reasonably based on transactions indicative of the actual value of the production in the area at that time.

3. GEOLOGIC SURVEY; ROYALTIES—Base Value—Computation.

   A lessee's obligation to pay royalty based on an accurate determination of the current value of production is not mitigated by its having committed by long-term contract to sell this product at a price below this value.

4. FEDERAL EMPLOYEES AND OFFICERS; GEOLOGIC SURVEY; INDIAN LANDS—Tribal Lands; REGULATIONS—Applicability; ROYALTIES—Base Value—Computation; RULES OF PRACTICE—Laches.

   Where Geological Survey did not expressly state otherwise, under its policy established and in effect since 1958, royalty payments are accepted subject to post audit and correction and do not necessarily constitute payments in full of royalty obligations. The Area Supervisor's silence does not imply acceptance; nor does his inaction bar the Government from asserting the incorrectness of the payment subsequently.

5. GEOLOGIC SURVEY; INDIAN LANDS—Tribal Lands; REGULATIONS—Applicability—Interpretation; ROYALTIES—Base Value—Computation.

   The Area Supervisor has the authority to require a lessee to determine the value of the lease product by both the "BTU" and "net realization" methods and may require the lessee to adopt as value whichever result is higher as the basis for computation of royalty for natural gas.

6. GEOLOGIC SURVEY; ROYALTIES—Base Value—Computation; RULES OF PRACTICE—Res Judicata.

   Where a United States District court has ordered a lessee to adopt a dual accounting method of determining value and has ordered the Department to require this dual accounting from the lessee, the question of the propriety of the Area Supervisor's order doing so is apparently res judicata, the only question being whether the order is the court's final action.

7. GEOLOGIC SURVEY; INDIAN LANDS—Tribal Lands; REGULATIONS—Applicability—Interpretation; ROYALTIES—Base Value—Computaton.

   Under controlling provisions, an Area Supervisor has the discretion to establish a cost-of-manufacture allowance for use in the net-realization method of determining value for royalty purposes. Where this allowance is well based on the actual amounts needed to process out by-products of the crude gas, it will be upheld in the absence of a clear showing that it is erroneous.

APPEARANCES: Bruce D. Black, Esq., and William S. Jameson, Esq., Santa Fe, New Mexico, for Supron Energy Corp.; Don Crestman, Esq., Forth Worth, Texas, for Southland Royalty Co.; Robert Rosnick, Esq., Denver, Colorado, for Consolidated Oil and Gas Co.; Harold L.

Hensley, Jr., Esq., Roswell, New Mexico, for Exxon Co., U.S.A.; Jason Kellahin, Esq., Santa Fe, New Mexico, for Atlantic Richfield Co., Continental Oil Co., and Tenneco Oil Co.; Robert J. Nordhaus, Esq., Albuquerque, New Mexico, for amicus curiae Jicarilla Apache Tribe; William R. Murray, Jr., Esq., Office of the Solicitor, for the Deputy Commissioner, Indian Affairs.

OPINION BY ADMINISTRATIVE JUDGE STUEBING

Supron Energy Corp. (Supron) and each of the other appellants (lessees), holders of Jicarilla tribal oil and gas leases producing large volumes of natural gas and related products, have appealed from decisions by the Acting Deputy Commissioner, Indian Affairs (the Deputy Commissioner), issued between December 1978 and March 1979.[1] Owing to the similarity of the subject matter presented in these appeals, we have consolidated them for consideration.

At various times on and after December 9, 1976,[2] the Area Oil and Gas Supervisor (Area Supervisor), Albuquerque, New Mexico, of the Geological Survey (GS), issued letter orders to lessees directing them to recompute royalties due on all Jicarilla tribal leases for the years 1971 through 1973 on the basis of specified minimum prices for each thousand cubic feet (mcf) of natural gas produced from them. As GS has subsequently explained, these minimum prices were to preempt any lower sale prices actually reported on any monthly reports of sales during this 3-year period, but were not to replace any higher prices on these reports. Thus, the Area Supervisor established floor prices for gas produced from these leases. The enunciated basis for his decision was that a detailed review of the gas pricing on all Jicarilla tribal leases for these years disclosed that the major portion of gas from

[1] *See* appendix.

[2] *See* appendix.

these leases was sold at prices equal to or higher than the amounts specified as minimums for these years. Finally, lessees were ordered to remit any additional royalties due under this method.

Lessees appealed the Area Supervisor's orders to the Director, GS, and the Commissioner of Indian Affairs, pursuant to 30 CFR 221.66 and Part 290. Between December 20, 1978, and March 8, 1979, the Deputy Commissioner issued six decisions disposing of these appeals, in which he affirmed the Area Supervisor's orders establishing minimum prices as they affected all of the lessees.[3] Lessees appealed these decisions to this Board, challenging the imposition of minimum floor prices for gas by which to redermine royalty.

On December 10, 1976, the Area Supervisor issued an order directing Supron to initiate computation of value under both the "BTU" (British Thermal Unit") and "net-realization" methods for the years 1974 through 1976 and to redetermine royalty based on the method yielding the higher value. Additionally, the Area Supervisor specified amounts to be used by Supron as cost-of-manufacture allowances under the net-realization method for each of these years. On December 13, 1976, the Area Supervisor ordered Supron to adopt the minimum floor prices discussed above. Supron appealed both of these orders.

In the decision concerning Supron's appeal (IND-10-O&G), the Deputy Commissioner held that the Area Supervisor's order establishing floor prices was correct, but he remanded the matter to the Area Supervisor for further documentation concerning the order which directed Supron to adopt the "BTU" and "net-realization" methods. Specifically, the Deputy Commissioner noted that the records failed to show the elements of cost of manufacture used to determine the allowance specified in this order. Accordingly, he directed the Area Supervisor to explain

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[3] *See* appendix.

to Supron how he had computed these allowances and why he did not adopt two-thirds of the value of the marketable products as the cost of manufacture, as provided in 25 CFR 171.13(a).

The Jicarilla Apache Tribe, as lessor of the subject leases attempted to intervene in the proceeding before the Deputy Commissioner to review the Area Supervisor's decisions, but its request was denied. The tribe also moved this Board for leave to appear in these appeals, but only as amicus curiae, and we granted this motion on July 9, 1979. However, we note that almost certainly we would have granted the tribe's full status to intervene as a party, had it so moved, in light of its direct interest in the resolution of these appeals.

We note initially that the "administrative records" submitted to this Board by GS in connection with these appeals are grossly incomplete. For example, they do not contain copies of the Area Supervisor's letter orders, from which the appeals directly followed. But for the inclusion of copies of these orders by lessees, we would have no idea when the orders were issued or what their contents were. The files contain no information prior to the filing of appeals by the lessees from the Area Director's decisions. Again, but for the diligence of the Solicitor in assembling the facts on which the Area Supervisor based these orders, we would have no basis on which to review their correctness. Finally, they do not contain several of the notices of appeal to this Board which lessees apparently filed with the Deputy Commissioner.

[1] The first issue here, which affects all lessees, is whether the Area Supervisor had authority to specify minimum floor prices for gas produced on these leases for the purpose of determining value and, if so, whether his determination of these values were correct. The regulation, 25 CFR 171.13(a), grants the Area Supervisor broad power in determining the value of oil and gas produced from leases on which royalty is calculated:

§ 171.13 Rates of rentals and royalties under oil and gas leases.

(a) The lessee shall pay, beginning with the date of approval of oil and gas leases by the Secretary of the Interior, * * * during the continuance, thereof, * * * a royalty of 12½ percent [4] of the value or amount of all oil, gas, and/or natural gasoline, and/or all other hydrocarbon substances produced and saved from the land leased, save and except oil, and/or gas used by the lessee for development and operation purposes on the lease, which oil or gas shall be royalty free. * * * During the period of supervision, "value" for the purposes of the lease may, in the discretion of the Secretary of the Interior, be calculated on the basis of the highest price paid or offered (whether calculated on the basis of short or actual volume) at the time of production for the major portion of * * * gas, and/or natural gasoline, and/or all other hydrocarbon substances produced and sold from the field where the leased lands are situated, and the actual volume of the marketable product less the content of foreign substances as determined by the supervisor. The actual amount realized by the lessee from the sale of said products may, in the discretion of the Secretary of the Interior, be deemed mere evidence of or conclusive evidence of such value. * * * In determining the value for royalty purposes of products, such as natural gasoline, that are derived from treatment of gas, a reasonable allowance for the cost of manufacture shall be made, such allowance to be two-thirds of the value of the market-

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[4] The Solicitor has furnished us with copies of leases No. 9 and 455, which are apparently the oldest and newest leases in question here. Lease No. 455 specifies a royalty rate of 16⅔ percent. By quoting the regulations and lease terms, we make no comment as to what specific royalty rate may be applicable in any of the leases here.

able product unless otherwise determined by the Secretary of the Interior on application of the lessee or on his own initiative, and that royalty will be computed on the value of gas or casing-head gas, or on the products thereof (such as residue gas, natural gasoline, propane, butane, etc.), whichever is the greater.

Sections 3(c) and (d) of the tribal lease terms also expressly address this question:

> (c) Rental and royalty.—To pay * * * a royalty of 12½ percent [5] of the value or amount of all oil, gas, and/or natural gasoline, and/or all other hydrocarbon substances produced and saved from the land leased herein, save and except oil, and/or gas used by the lessee for development and operation purposes on said lease, which oil or gas shall be royalty free. During the period of supervision, "value" for the purposes hereof may, in the discretion of the Secretary, be calculated on the basis of the highest price paid or offered (whether calculated on the basis of short or actual volume) at the time of production for the major portion of the oil of the same gravity, and gas, and/or natural gasoline, and/or all other hydrocarbon substances produced and sold from the field where the leased lands are situated, and the actual volume of the marketable product less the content of foreign substances as determined by the oil and gas supervisor. The actual amount realized by the lessee from the sale of said products may, in the discretion of the Secretary, be deemed mere evidence of or conclusive evidence of such value. * * * It is understood that in determining the value for royalty purposes of products, such as natural gasoline, that are derived from treatment of gas, a reasonable allowance for the cost of manufacture shall be made,

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[5] *See* n.4, *supra*.

such allowance to be two-thirds of the value of the marketable product unless otherwise determined by the Secretary of the Interior on application of the lessee or on his own initiative, and that royalty will be computed on the value of gas or casinghead gas, or on the products thereof (such as residue gas, natural gasoline, propane butane, etc.), whichever is the greater.

(d) Monthly statements.—To furnish to the oil and gas supervisor monthly statements in detail in such form as may be prescribed by the Secretary of the Interior, showing the amount, quality, and value of all oil, gas, natural gasoline, or other hydrocarbon substances produced and saved during the preceding calendar month as a basis upon which to compute, for the treasurer of said tribe or the superintendent, the royalty due the lessor. The leased premises and all wells, producing operations, improvements, machinery, and fixtures thereon and connected therewith and all books and accounts of the lessee shall be open at all times for the inspection of any duly authorized representative of the Secretary of the Interior.

Under these provisions, the Area Supervisor is given considerable latitude in determining what is the "value" of the production from a lease. *Amoco Production Co.*, 29 IBLA 234, 236 (1977).* He may simply adopt as conclusive the actual amount which a lessee receives from sales of the leased product as its "value," or may, in his discretion, go so far as to take the highest price paid or offered for the major portion of the gas produced and sold from the field where the leased lands are located as "value"—a figure which might be substantially higher than the actual sale price.

Under the regulations applying generally to all oil and gas leases controlled by the United States, the Area Su-

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*GFS (O&G) 35 (1977)

pervisor may impose the value of production for computing royalty in which he determines is "reasonable," duly considering the highest price paid for a part or majority of production of like quality in the same field. 30 CFR 221.47.

[2] Nevertheless, it must appear on review that there is a reasonable basis in fact for his decision to set value other than at the actual price received. In the instant case, the Area Supervisor assembled complete sales data from all Jicarilla tribal leases for the years 1971 through 1973. He then determined the median price for all gas sold from these leases in each calendar year, that is, the price at which, or above which, half of the gas was sold and, at the same time, the price at which, or below which, the other half was sold. For example, in 1971, 49,282,772 mcf of gas were sold from all of the Jicarilla leases. The median price from these sales was $0.15, meaning that 24,641,386 mcf were sold at this price or higher, and 24,641,386 mcf were sold at this price or lower. Thus, the figures adopted by the Area Supervisor are based on actual production figures. The Area Supervisor adopted these median prices as the floor values of gas for each year, that is, he held that the "value" of the gas throughout each year was *not less than* these median values.

The use of the yearly median in this manner as the floor value for that year is within the discretionary latitude granted to the supervisor by the regulations. The median is not necessarily the "highest price paid or offered for the major portion of" the gas. For example, it is possible that the prices *offered* for the gas were higher than the actual prices paid for it. However, it should be remembered that the figures adopted by the supervisor are not replacements for the actual sales prices, but are floors beneath which these values may not be calculated. Thus, the lessees must still report and use the actual prices if they are above these floors and may well pay royalty based on a value higher than the sale price

actually received. Sales prices may not always reflect true value. Therefore, it is not unreasonable to impose a floor value which is less than the highest value which the regulations would permit.

The Area Supervisor was justified in demanding that value be reported as the monthly proceeds from sales where these proceeds are *greater* than the specified minimum floor price. Under 30 CFR 221.47, the value of production for royalty purposes must be at least equal to the actual proceeds accruing to the lessee upon sale of the output of the lease. *Amoco Production Co., supra* at 236; *Wheless Drilling Co.* 13 IBLA 21, 80 I.D. 559 (1973);[b] *see California Co.* v. *Udall*, 296 F.2d 384 (D.C. Cir. 1961). This would not be so if the minimum floor price were accepted when actual sales proceeds were higher.

[3] By establishing floor values based on actual sales data of similar products, the Department prevents a lessee from avoiding its obligation to pay a fair royalty to the owners of the leased resources. It is irrelevant that the sales prices which fall below these floor values are set by long-term contract. The lessee may not avoid its responsibility to pay a fair royalty because it has made long-term commitments. The regulations clearly allow the superimposition of the Area Supervisor's determination of values based on actual market conditions on any sales prices which fall below this standard and make no provisions for exempting production from leases which is subject to pre-existing long-term pricing.

[4] Lessees each contend that the Department, by accepting their monthly reports which state that the value was the actual sales price, and has exercised its discretion and elected to consider these prices as conclusive evidence of such value, so that it may not change the value on which royalty is computed. This argument is not persuasive.

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[b] GFS (O&G) 82 (1973)

In 1958 GS adopted the practice of billing lessees for royalty on the basis of the information contained in monthly reports which they submitted, *subject to post audit. Big Piney Oil and Gas Co.*, A-29895 (July 27, 1964).[c] According to the affidavit of the Chief Accountant, Conservation Division, GS, this procedure is still in effect today and was at all times in question: The statements of account (bills) generally reflected only the information on value supplied by the lessees, except for automatic rental or minimum royalty charges, and correction of obvious errors. The statements contained no independent vertification by GS personnel as to value of the production of the lease (Sol. Brief, Exh. A).

In the absence of acceptance of the lessee's statement of value as conclusive by any official authorized to bind the Department contractually, the Department is not barred from rejecting this statement as incorrect, determining value by another acceptable method, and demanding payment of royalty based on this method. *Big Piney Oil and Gas Co., supra.* Otherwise, there must be an *express* commitment to accept a certain amount of royalty, and an Area Supervisor's silence on the question of how much royalty is due implies no such commitment. *Sinclair Oil and Gas Co.*, 75 I.D. 155, 172-3 (1968).[d]

The monthly statements do not indicate or suggest that the amounts charged therein are final determinations of the royalty due. Appellants have shown nothing to indicate that the Department explicitly indicated that these statements would finally establish value. Therefore, we find that the Department's first explicit action to determine value officially was taken when the Area Supervisor issued the orders here. No election by the Department to

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[c] GFS (O&G) SO-73 (1964)

[d] GFS (O&G) SO-14 (1968)

accept the actual sales prices as representative of true value occurred previously.[6]

Nor does the delay in taking this first action affect its validity. The authority of the United States to protect a public interest, including its obligation to protect the ownership rights of the Jicarilla Apaches, is not vitiated or lost by its employees' laches, failure to act, or delays in the performance of their duties. 43 CFR 1810.3(a). Lessees could not properly have relied on the Area Supervisor's failure to act. *Sinclair Oil and Gas Co., supra.*

Our holding is in conformity with the realities of administering the collection of lease royalties. When GS receives a lessee's monthly statement of value, it cannot immediately know what the sales data for the entire field are, and it will necessarily take time to assemble this information and interpret it. Inaction during this time could reasonably indicate that the Department is considering whether to adopt these sales prices as adequate for "value" or, instead, to impose its own determination thereof on the lesses.

Lessees cite *Continental Oil Co.* v. *United States*, 184 F.2d 802, 821 (9th Cir. 1950) for the proposition that the Department may not reassess royalty at a value in excess of that previously determined and billed by the Department. In *Continental*, the Department issued an order on June 4, 1931, which recited that the value of gas produced from leases in California would be $0.05 per mcf and that the value of natural gasoline would be

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[6] We do not imply that such explicit approval of royalty payment would necessarily bind the Government in all cases. Where the Department directs lessees (even explicitly) to compute royalty in a manner which is beyond its authority to allow, it is *not* estopped by its acceptance of the erroneous payments from correcting its error. *Atlantic Richfield Co.* v. *Hickel*, 432 F.2d 587, 591 (10th Cir. 1979). In the instant case, we do not imply that royalties may not be increased further if it is finally determined judicially that the Department was without authority to compute value in this manner.

$0.06 below the San Francisco price for tank-wagon lots, or alternatively would be the amounts actually received by the lessees, if greater than the former amounts. This order was changed on June 23, 1931, to tie the floor value of gasoline to the retail market, but no change in the fixed minimum value of gas was ordered. *United States* v. *General Petroleum Corp.*, 75 F. Supp. 225, 232 (S.D. Cal. 1946), *aff'd*, *Continental Oil Co.* v. *United States*, *supra*. On June 7, 1937, more than 6 years after making this official announcement on how the values of lease products would be determined, the Department issued another order again altering this policy to introduce the "net-realization" method of accounting as an alternative to the "actual-price-above-specified-minimum" method in effect since 1931. *Ibid.*

Before the Ninth Circuit, the Department argued that it could not only apply the 1937 method to collect royalties on production realized after the effective date of the ordering establishing it, but could also use it to recompute royalties from production realized *before* this date where the lessee had not yet paid them. In the section cited by lessees, the Ninth Circuit held that the method adopted in 1937 could be applied prospectively only and not to production between 1931 and its issuance.

In *Continental*, the Department had expressly elected a method of valuation of lease products in June 1931 and had officially ordered lessees to adopt it. The instant case is materially different, in that, as noted above, the Department made no such election until 1976 and 1977. Unlike in *Continental*, where the Department was attempting to *reassess* value retroactively, the Department made its *initial* assessment of value here, although it was made after the sales in question. The Ninth Circuit's rule in *Continental* is consistent with that in *Big Piney*, *supra*: Where the Department *has not* specified that a particular method of valuation adopted by a lessee is adequate, it *may* assert that the method is incorrect and redetermine royalty after the sales, even though payment

has already been accepted (*Big Piney*); where the Department *has* specified that a method of valuation is adequate, it *may not* assert that this method is incorrect or incomplete and reassess value retroactively in order to raise the royalty due, even though payments have not been tendered (*Continental*).

Thus, *Continental* does not support lessees' position. To the contrary, it stresses that the issuance and communication of a Departmental policy decision regarding how value is to be determined will settle the question for all production until the decision is superceded by another determination. Thus, the policy announced in 1958 and enforced by the Department in *Big Piney*, *supra* (under which the Department bills lessees for royalty on the basis of information submitted by them, reserving the right later to reject the billed amounts as incorrect, in the absence of express acceptance of this amount), still stands, as lessees make no suggestion that it was superceded by any other Departmental policy statement.

We also reject lessees' argument that the Area Supervisor's orders are not final in that they set a minimum value for royalty but fail to set a maximum, and so avoid the final determination of value and leave the way open for further determinations. This is simply not true. The import of the orders is that the amount on which royalty must be determined is either the price specified in the order for a particular year, or the price at which the gas was actually sold, whichever is greater. There is no uncertainty or lack of finality in this, as both price figures are known. The orders might well have been phrased in a way which would have made this result clearer, but it is difficult to believe that lessees retain any bona fide doubt as to what the directive means at this stage of the proceeding.[7]

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[7] As noted above at n.6, in holding that these orders were final, we simply hold that they required definite action by lessees which was not subject to later revision. We do not imply that lessees will

Atlantic Richfield Co. (Arco), Continental Oil Co., and Tenneco Oil Co., argue that the Area Supervisor erred by considering all gas sales from the reservation, including both intrastate sales and interstate sales under regulated prices. They note the price at which the major portion of gas sold would be lower than he found if he had considered only the intrastate market, which they feel is a more competitive, and therefore more representative, marketplace. The regulations and lease terms allow the Area Supervisor to consider the actual prices of the gas, etc., sold from the entire field, without regard to the type of market in which the products are sold. Thus, as we have held above, the Area Supervisor was within his discretion in basing his determination of value on all sales from Jicarilla leases. This information necessarily concerned sales in both the inter- and intra-state markets and was therefore representative of the actual proceeds received by lessees, who admittedly sold the gas in both markets. Moreover, the Area Supervisor has the authority to use the highest price paid as his guide. Thus, he was within his authority in declining to use the intrastate price, as it was admittedly not the highest pricing guide available.

The case cited in Arco's brief in support of this argument, *Hemus* v. *Hawkins*, 452 F. Supp. 861 (S. D. Texas 1978), is not in point. This matter was a suit to enforce a *private* royalty arrangement under which royalty was computed on the "market value" of the lease product and so does not relate to the terms under which Federal royalties are determined. In any event, the holding there that intrastate prices should be used in computing the "market value" was based on the fact that all of the production in question was sold intrastate. Such is not the case here.

Exxon Co., U.S.A. (Exxon), has challenged the propriety of ordering it to amend its royalty payments, stating

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not be subject to judicial or administrative orders increasing the valuation of the products in question in the event that it is determined that these orders were inadequate to establish value correctly.

that it has only a nonoperating interest and that Supron had agreed to perform its obligations to pay royalty. It is inappropriate to consider what the arrangeemnt between Exxon and Supron may have been regarding Supron's assuming the responsibility of paying royalty due under Exxon's share of the leases. As Exxon admits, it was the lessee of record during the time in question. As such, it is responsible for payment of the correct royalty due, and the Area Supervisor was without fault in informing it of this responsibility.

[5] Up to this point, this opinion has considered only one method of determining the value of production from a lease, that is, the method where the actual sales price of the product, not less than specified floor prices, determines its value. There are two other means of determining value in question: the "BTU" and "net-realization" methods. In the former, the volume of the crude gas stream is measured at the wellhead (after casinghead gasoline is removed) and the BTU value of the gas stream is periodically measured. Then, the volume is multiplied times the price of gas per mcf, which result is in turn multiplied by an adjustment factor to account for its BTU content, giving the value under the BTU method. In the "net-realization" method, the values of the component parts of the gas stream (gasoline, propane, butane, ethane, etc., and the residue gas remaining after these products are removed) are determined after they have been separated from the gas stream by processing. The aggregate of the values of these component parts is determined and an allowance for the cost of manufacturing (separating) the component parts is subtracted from it. The difference is regarded as the value under the net-realization method, being the net value of the products realized from the crude gas stream.

Supron has appealed from the Area Supervisor's order of December 10, 1976, which requires it to make reports

of value for 1974 through 1976 by both the BTU and net-realization methods and submit royalty based on the method yielding the higher value. Although it is not clear in this order, we presume that the Area Supervisor was also directing Supron to compare the values resulting from these two methods with the actual price received for the gas, and to pay method royalty based on the highest to these three figures. (N.B. that it appears that no minimum floor value has been set for 1974 through 1976.) Additionally, the Area Supervisor directed Supron to use specific cost-of-manufacture allowances for these years. Supron has challenged the authority of the Area Supervisor to direct it to use these methods and the validity of these specified yearly cost-of-manufacture allowances.

There is no question that the Area Supervisor had the authority to require Supron to compute value under the BTU and net-realization methods, and to require it to submit the highest royalty determined from these methods or from actual prices. The provisions of 30 CFR 221.47 clearly justify the BTU method, providing that the value of production for computing royalty shall in no circumstances be deemed to be less than the value computed on such reasonable unit value as the Area Supervisor determines on behalf of the Secretary. Similarly, section 3(c) of the leases notes that royalty will be computed on the value of gas. The BTU method measures the value of gas by effectively applying the price rate per BTU and so directly follows these provisions.

Use of the net-realization method is also clearly authorized. Section 3(c) of the leases notes expressly that royalty may be computed on the value of products of gas such as natural gasoline, propane, butane, and residue gas, and that the royalty due shall be the greater of the two amounts determined by this and the value-of-gas (BTU) methods. The provisions of 30 CFR 221.50 implicitly justify using the net-realization method as well, in that they refer to determining royalty on the basis of the

value of dry gas remaining after the extraction of gasoline (30 CFR 221.50(a)) and to the aggregate value of all commodities obtained from the product (30 CFR 221.50(c)). Section 3(c) of the leases and 25 CFR 171.13(a) both specify a discretionary two-thirds cost-of-manufacture allowance to be used in determining the aggregate value of component parts derived from treatment of the product.

Thus, computation of royalty by the higher of the two values determined by the BTU and net-realization methods is well recognized in the regulations and lease terms. Accordingly, we conclude that it was proper for the Area Supervisor to require Supron to do so.

[6] Even were we to disregard the presence of this authorization to use this dual accounting method, we would be constrained to affirm the Area Supervisor's decision in view of the interim holding of the United States District Court for the District of New Mexico in *The Jicarilla Apache Tribe* v. *Supron Energy Corp., et al.*, No. 75-247-M (November 5, 1979), which *inter alia*, orders Supron to utilize the dual accounting system. Inasmuch as this action addresses this issue directly, and as Supron and the Department are both parties to it, the question of the imposition of the dual accounting requirement is apparently res judicata, the only question remaining being whether the opinion cited is the final order of the District Court for the District of New Mexico.

It remains to decide whether the Area Supervisor's decision imposing a specific cost-of-manufacture allowance for 1974 through 1976 was correct. The regulations, 25 CFR 171.13(a), and the lease terms, section 3(c), authorize the Area Supervisor, as the Secretary's representative (*see* 30 CFR 221.2(c) and 221.3), to grant two-thirds of the value of the marketable component parts of the gas as a cost-of-manufacture allowance, to be deducted from the receipts from the sales of these component parts

to give the agregate value for royalty purposes. However, he is also granted the discretion to determine otherwise if appropriate. Thus, even though as Supron alleges, the two-thirds allowance may be standard in the oil and gas industry, the Area Supervisor clearly has the authority to establish a different allowance if he has a reasonable basis for doing so.

On his review of these matters, the Deputy Commissioner was not satisfied that the record showed that the allowance which the Area Supervisor established was correct and accordingly remanded the case to him for explanation of the basis of this decision. The Area Supervisor responded immediately by writing directly to Supron with data supporting his conclusion as to the specific cost-of-manufacture allowance for 1974 and 1975, but he did not address the quoted figure for 1976. No copy of this material was placed in the administrative record by the Supervisor, but Supron has included the original letter as Exhibit D to its statement of reasons.

We are satisfied that the Area Superisor's decision to establish specific allowances for 1974 and 1975 is well based in fact, and we conclude that it is accurate. On April 15, 1976, the Area Supervisor notified Supron that he was required to monitor accounting on both the BTU and the net-realization methods, and that he would be redetermining the cost-of-manufacture allowance used in the latter method. Accordingly, he requested that Supron provide him with specific data and enclosed a copy of the guidelines to be used for doing so.

In his letter to Supron, pursuant to the Deputy Commissioner's decision, the Area Supervisor explained that he used this data in determining the specific allowances for 1974 and 1975 and showed exactly how he did so. In the absence of a clear demonstration that this methodology was incorrect, it is entitled to our deference, as the Area Supervisor has been duly delegated the authority to make

this determination and is well familiar with the particulars of oil and gas production. *See Rosita Trujillo,* 21 IBLA 289, 191 (1975).*

In any event, we are satisfied that it is an accurate and liberal method of determining the cost-of-manufacture allowance. It takes into account production and maintenance expenses, depreciation, and grants an additional 10 percent allowance for administrative and general expenses. The result is a figure representing the cost of manufacturing each gallon of liquid product separated in the Lybrook Plant, which, at the time in question, was owned by Supron.

The Lybrook Plant apparently processed gas from many different sources, and the Area Supervisor's allowance is based on all processing done at this facility. Supron objects to the Area Supervisor's failure to identify specifically the cost of manufacture of the gas from the Jicarilla tribal leases. In the absence of a clear showing by Supron to the contrary, a plant-wide average is a reasonable means of determining the cost of processing a gallon of by product from the gas streams of the Jicarilla leases, and we accept it as valid. *Id.*

Supron also challenges the Area Supervisor's failure to give it credit for expenses incurred for State and Federal income taxes and for fuel costs or shrinkage, and proper credit for administrative and general expenses.

Inasmuch as it is determined by numerous factors, many of which are unrelated to operation, including income and/or losses from other sources, tax brackets, accounting methods, etc., income tax is not properly regarded as a cost-of-manufacture which may be deducted from gross receipts in order to determine the value of a product. It is proper to apply Federal income taxation principles to royalty determination questions. *See Amoco*

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* GFS (O&G) 94 (1975)

Production Co., supra at 237, n.1. Income taxes are imposed upon realized gain, not upon realized gain diminished by the amount of such taxes which ultimately may be found attributbale to the realized gain. *Taylor* v. *Commissioner of Internal Revenue*, 298 F.2d 198, 203 (4th Cir. 1962). So it is also with the imposition of royalty.

In fact, fuel costs and shrinkage are taken into account in the dual-accounting system. Royalty is determined on the basis of the volumes of products *leaving* the processing plant. These volumes are clearly diminished when gas is lost in transit to the plant or is used in processing. That is, if gas is lost in transit and/or consumed during processing, the amount of royalty will be reduced accordingly because the amount of product sold at the tailage of the plant will be reduced by an equivalent amount. Thus, the net-realization system automatically takes into account these factors. Of course, if an excessive amount of gas is lost and/or used for production, the lessee will not avoid paying royalty, as it will be charged alternatively on the basis of the actual-sales-price or wellhead volume (BTU) methods described above if they show a greater value.

Part 6477.3E(9) of the GS Conservation Division Manual specifies a maximum allowance of 10 percent of the permittee's operating and maintenance costs for general administrative costs such as telephone service, office supplies, etc. While this manual does not have the force of law, we will not disturb a decision based on it in the absence figures clearly showing that 10 percent of total expenses is inadequate as a credit for administrative and general expenses.

The part of this decision which requires Supron to calculate value under the BTU and net-realization methods and submit appropriate royalty payments for 1974 and 1975 is affirmed, and Supron is ordered to comply within 60 days of its receipt of this decision. However, the Area

Supervisor's explanation of the methodology used in arriving at the cost-of-manufacture allowances does not address how he determined this value for the year 1976. It is necessary that he do so before Supron is ordered to comply with his December 10, 1976, decision. Accordingly, the matter is remanded to the Area Supervisor so that he may offer the same type of explanation concerning the specified cost-of-manufacture allowance for 1976 as he presented for 1974 and 1975.

The Area Supervisor's decisions requiring all lessees to adopt minimum floor prices and recompute royalties as required for the years 1971 through 1973, and the Deputy Commissioner's decision affirming them, are also affirmed, and lessees are ordered to comply within 60 days from their receipt of this decision.

Therefore, pursuant to the authority delegated to the Board of Land Appeals by the Secretary of the Interior, 43 CFR 4.1, the decision appealed from is affirmed in part and remanded in part for clarification.

/s/ Edward W. Stuebing
EDWARD W. STUEBING
Administrative Judge

We concur:

/s/ Frederick Fishman
FREDERICK FISHMAN
Administrative Judge

/s/ James L. Burski
JAMES L. BURSKI
Administrative Judge

APPENDIX

IBLA No.	Lessees/ Appellants *	Deputy Commissioner's Decision No. (Docket No.)	Date	Dates of Area Supervisor's Order(s)
79-374	Supron Energy Corp.*	IND-10-O&G (IND 9)	1-16-79	12-10-76 12-13-76
79-390	Atlantic Richfield Co.	IND-13-O&G (IND 12)	3-8-79	3-18-77
	Continental Oil Co.	IND-15-O&G (IND 14)	3-8-79	12-10-76
	Tenneco Oil Co.	IND-15-O&G (IND 10)	3-8-79	12-14-76
79-420	Exxon Co., U.S.A.	IND-16-O&G (IND 13)	3-8-79	3-18-77
79-421	Southland Royalty Co.*	IND-9-O&G (IND 2)	12-20-78	12-9-76
79-427	Consolidated Oil and Gas Co.	IND-14-O&G (IND 3)	3-8-79	12-10-76

* These names are the lessees' current names. Supron Energy Corp. was formerly Southern Union Production Co.; Southland Royalty Co. was formerly Aztec Oil and Gas Co.

INDEX CODE:
25 CFR 171.13(a)
30 CFR 221.2(c)
30 CFR 221.3
30 CFR 221.47
30 CFR 221.50(a) and (c)
30 CFR 221.66
30 CFR Part 290
43 CFR 1810.3(a)

APPENDIX J

25 U.S.C.A. CH. 12 (1983)

INDIAN MINERAL LEASING ACT OF 1938

§ 396a. Leases of unallotted lands for mining purposes; duration of leases

On and after May 11, 1938, unallotted lands within any Indian reservation or lands owned by any tribe, group, or band of Indians under Federal jurisdiction, except those specifically excepted from the provisions of sections 396a to 396g of this title, may, with the approval of the Secretary of the Interior, be leased for mining purposes, by authority of the tribal council or other authorized spokesmen for such Indians, for terms not to exceed ten years and as long thereafter as minerals are produced in paying quantities.

(May 11, 1938, c. 198, § 1, 52 Stat. 347.)

§ 396b. Public auction of oil and gas leases; requirements

Leases for oil- and/or gas-mining purposes covering such unallotted lands shall be offered for sale to the highest responsible qualified bidder, at public auction or on sealed bids, after notice and advertisement, upon such terms and subject to such conditions as the Secretary of the Interior may prescribe. Such advertisement shall reserve to the Secretary of the Interior the right to reject all bids whenever in his judgment the interest of the Indians will be served by so doing, and if no satisfactory bid is received, or the accepted bidder fails to complete the lease, or the Secretary of the Interior shall determine that it is unwise in the interest of the Indians to accept the highest bid, said Secretary may readvertise such lease for sale, or with the consent of the tribal council or other governing tribal authorities, a lease may be made by private negotiations: *Provided,* That the foregoing provisions shall in no manner restrict the right of tribes

organized and incorporated under sections 476 and 477 of this title, to lease lands for mining purposes as therein provided and in accordance with the provisions of any constitution and charter adopted by any Indian tribe pursuant to sections 461, 462, 463, 464, 465, 466 to 470, 471 to 473, 474, 475, 476 to 478, and 479 of this title.

(May 11, 1938, c. 198, § 2, 52 Stat. 347.)

§ 396c. Lessees of restricted lands to furnish bonds for performance

On and after May 11, 1938, lessees of restricted Indian lands, tribal or allotted, for mining purposes, including oil and gas, shall furnish corporate surety bonds, in amounts satisfactory to the Secretary of the Interior, guaranteeing compliance with the terms of their leases: *Provided*, That personal surety bonds may be accepted where the sureties deposit as collateral with the said Secretary of the Interior any public-debt obligations of the United States guaranteed as to principal and interest by the United States equal to the full amount of such bonds, or other collateral satisfactory to the Secretary of the Interior, or show ownership to unencumbered real estate of a value equal to twice the amount of the bonds.

(May 11, 1938, c. 198, § 3, 52 Stat. 348.)

§ 396d. Rules and regulations governing operations; limitations on oil or gas leases

All operations under any oil, gas, or other mineral lease issued pursuant to the terms of sections 396a to 396g of this title or any other Act affecting restricted Indian lands shall be subject to the rules and regulations promulgated by the Secretary of the Interior. In the discretion of the said Secretary, any lease for oil or gas issued under the provisions of sections 396a to 396g of this title shall be made subject to the terms of any reasonable cooperative unit or other plan approved or prescribed by said Secretary prior or subsequent to the issuance of any such lease which involves the development

or production of oil or gas from land covered by such lease.

(May 11, 1938, c. 198, § 4, 52 Stat. 348.)

§ 396e. Officials authorized to approve leases

The Secretary of the Interior may, in his discretion, authorize superintendents or other officials in the Indian Service to approve leases for oil, gas, or other mining purposes covering any restricted Indian lands, tribal or allotted.

(May 11, 1938, c. 198, § 5, 52 Stat. 348.)

§ 396f. Lands excepted from leasing provisions

Sections, 396a, 396b, 396c, and 396d of this title shall not apply to the Crow Reservation in Montana, the ceded lands of the Shoshone Reservation in Wyoming, the Osage Reservation in Oklahoma, nor to the coal and asphalt lands of the Choctaw and Chickasaw Tribes in Oklahoma.

(May 11, 1938, c. 198, § 6, 52 Stat. 348; May 27, 1955, c. 106, § 2, 69 Stat. 68.)

396g. Subsurface storage of oil or gas

The Secretary of the Interior, to avoid waste or to promote the conservation of natural resources or the welfare of the Indians, is authorized in his discretion to approve leases of lands that are subject to lease under section 396 or 396a of this title, for the subsurface storage of oil and gas, irrespective of the lands from which initially produced, and the Secretary is authorized, in order to provide for the subsurface storage of oil or gas, to approve modifications, amendments, or extensions of the oil and gas or other mining lease(s), if any, in effect as to restricted Indian lands, tribal or allotted, and may promulgate rules and regulations consistent with such leases, modifications, amendments, and extensions, relat-

ing to the storage of oil or gas thereunder. Any such leases may provide for the payment of a storage fee or rental on such stored oil or gas or, in lieu of such fee or rental, for a royalty other than that prescribed in the lease when such stored oil or gas is produced in conjunction with oil or gas not previously produced. It may be provided that any oil and gas lease under which storage of oil or gas is so authorized shall be continued in effect at least for the period of such storage use and so long thereafter as oil or gas not previously produced is produced in paying quantities.

(May 11, 1938, c. 198, § 8, as added Aug. 1, 1956, c. 808, 70 Stat. 774.)

Calendar No. 1019

75th Congress SENATE Report
1st Session No. 985

LEASING INDIAN LANDS FOR MINING PURPOSES

JULY 22 (calendar day, JULY 28) 1937.—Ordered to be printed

Mr. THOMAS of Oklahoma, from the Committee on Indian Affairs, submitted the following

REPORT

[To accompany S. 2689]

The Committee on Indian Affairs, to whom was referred the bill (S.2689) to regulate the leasing of certain Indian lands for mining purposes, having considered the same, report thereon with the recommendation that it do pass without amendment.

The proposed legislation was suggested by the Secretary of the Interior in a communication dated June 17, 1937, addressed to the President of the Senate, who referred the same to your committee for consideration; thereafter, your committee authorized the introduction of a bill (S. 2689) for the purpose of carrying out the wishes of the Secretary of the Interior, and thereupon said bill (S. 2689) was referred to your committee for further consideration.

The communication of the Secretary of the Interior, dated July 17, 1937, above referred to, is attached hereto and made a part of this report, as follows:

DEPARTMENT OF THE INTERIOR,
Washington, June 17, 1937.

The PRESIDENT OF THE SENATE.

MY DEAR MR. PRESIDENT: I transmit herewith a proposed bill to govern the leasing of Indian lands for mining purposes.

Under section 26 of the act of June 30, 1919 (41 Stat. 31), as amended, leases for minerals other than oil and gas may be made on any reservation in the States of Arizona, California, Idaho, Montana, Nevada, New Mexico, Oregon, Washington, or Wyoming. Under the provisions of section 3 of the act of February 28, 1891 (26 Stat. 785), as amended May 29, 1924 (43 Stat. 244), leases for oil, gas, and other minerals may be made with the consent of the tribal council on treaty reservations in all States. Section 16 of the Indian Reorganization Act, approved June 18, 1934 (46 Stat. 984), provides that organized Indian tribes shall have the power to prevent the leasing of tribal lands. Under section 17 of that act Indian tribes to which charters of incorporation issue are empowered to lease their lands for periods of not more than 10 years. There is at present no law under which Executive-order lands may be leased for mining, outside of the States mentioned in the act of June 30, 1919, except for oil and gas mining purposes, unless the tribes are hereafter qualified under sections 16 and 17 of the Indian Reorganization Act. One of the purposes of the legislation now proposed, therefore, is to obtain uniformity so far as practicable of the law relating to the leasing of tribal lands for mining purposes.

The act of June 30, 1919 requires the formal opening of lands for prospecting, location, and lease, by the Secretary of the Interior, before an application for a lease for minerals other than oil and gas can be considered. It also requires that a person desiring to lease shall locate the mining claims as under the United States mining

laws, file formal location notice; and under the regulations he must have the lands surveyed if they have not already been surveyed, all in accordance with the mining laws applicable to the public domain. This frequently results in long delay and is often quite an expense to an applicant for a lease. Frequently we have requests for leases for the purpose of removing sand and gravel for roadgrading purposes, or for the quarrying of stone, either for building or grading purposes in connection with which there would be little or no under-surface workings. In such cases, applicants for leases are required to go through all the formality and expense necessary to acquiring actual mining leases. Sometimes the time and expense of making the locations and of having the land surveyed are more than they care to undertake although the material desired may be very conveniently located and could be profitably utilized; and consequently the opportunity to lease the land is lost and the revenue, while perhaps not a great deal in a particular instance would amount to considerable in such cases through the entire Indian Service.

Section 26 of the act of June 30, 1919, *supra*, as amended by the acts of March 3, 1921 (41 Stat. 1231), and December 16, 1926 (44 Stat. 922-923), places unallotted Indian lands within the States mentioned therein upon the same basis for prospecting and leasing for metalliferous minerals as lands of the public domain, after such Indian reservation lands have been declared opened by the Secretary of the Interior. It has been held that the Secretary of the Interior has no discretion under the said section in the matter of granting a lease to an applicant who has properly located his claim and complied with the laws and regulations of the Department thereunder; and in several instances it has been necessary to grant the lease notwithstanding the fact that the Indians of the reservation were opposed to leasing the lands. In other words, under that law, neither this Department nor

the Indian Tribal Council is in a position to prevent the acquisition of a lease after the lands have been declared open to prospecting and lease, and the Indians at no time have any voice in the granting of such leases.

It is not believed that the present law is adequate to give the Indians the greatest return from their property. As stated, present law provides for locating and taking mineral leases in the same manner as mining locations are made on the public lands of the United States; but there are disadvantages in following this procedure on Indian lands that are not present in applying for a claim on the public domain. For instance, on the public domain the discoverer of a mineral deposit gets extralateral rights and can follow the ore beyond the side lines indefinitely, while on the Indian lands under the act of June 30, 1919, he is limited to the confines of the survey markers not to exceed 600 feet by 1,500 feet in any one claim. The draft of the bill herewith would permit the obtaining of sufficient acreage to remove the necessity for extralateral rights with all its attending controversies.

The most urgent change is in the interest of leasing deposits of building stone, sand, gravel, and metalliferous minerals. For instance, the well-known iron deposit on the Fort Apache Indian Reservation, outcropping along the canyon wall for a distance of about 2 miles and 20 feet thick, with an estimated ore reserve of over 15 million tons, now must be "discovered" and located and monumented and then an application made for a lease. Under the present law only the outcrop along the canyon wall can be taken up under the lease as there are no outcrops of iron ore back from the face of the cliff. This deposit, it is believed, could be leased to better advantage at public auction and in definite areas rather than to anyone who erects a few monuments along the outcrop and applies for a preference right to a lease, through tieing up the land with a long strip 600 feet wide. This deposit of iron ore is about 30 miles from a railroad, and any-

one interested and considering building a railroad and developing the property would want a reserve greater than 600 feet back from the edge of the cliff. This deposit should appropriately be laid out in blocks extending at least 1 mile back from the outcrop.

Coal deposits on the several reservations are not adaptable to the discovery and location feature of the present act, which has very limited application. The presence of coal is usually known by geological association, and leases may be made with reasonable assurance before any coal is actually exposed on the land. Deposits of marl along the west side of Pyramid Lake, Nev., can be seen for a distance of many miles, yet they must be "discovered" and "located" in accordance with the provisions of law relating to placer mining claims and leased to the person who erects monuments thereon. Deposits of sand, gravel, and building stone are now similarly leased, even though the deposits are well known and could be leased with greater advantage to the Indians in definite areas.

The attached draft of bill, it is believed, would be a more satisfactory law for the leasing of Indian lands for general mining purposes. It will bring all mineral leasing matters in harmony with the Indian Reorganization Act, and I recommend that it be enacted.

The Acting Director of the Bureau of the Budget has advised that there is no objection to the presentation of this report to the Congress.

Sincerely yours,

CHARLES WEST,
Acting Secretary of the Interior.

HOUSE OF REPRESENTATIVES
75th Congress — Report
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LEASING INDIAN LANDS FOR MINING PURPOSES

MARCH 3, 1938.—Committed to the Committee of the Whole House on the state of the Union and Ordered to be printed

Mr. ROGERS of Oklahoma, from the Committee on Indian Affairs, submitted the following

REPORT

[To accompany H. R. 7626]

The Committee on Indian Affairs, to whom was referred the bill (H. R. 7626) to regulate the leasing of certain Indian lands for mining purposes, having considered the same, report thereon with a recommendation that it do pass without amendment.

This proposed bill received the unanimous vote of your committee.

The proposed legislation was suggested by the Secretary of the Interior as can be seen by the following letter addressed to the Speaker of the House of Representatives:

DEPARTMENT OF THE INTERIOR,
Washington, June 17, 1937.

The SPEAKER OF THE HOUSE OF REPRESENTATIVES.

MY DEAR MR. SPEAKER: I transmit herewith a proposed bill to govern the leasing of Indian lands for mining purposes.

Under section 26 of the act of June 30, 1919 (41 Stat. 31), as amended, leases for minerals other than oil and gas may be made on any reservation in the States of Arizona, California, Idaho, Montana, Nevada, New Mexico, Oregon, Washington, or Wyoming. Under the provisions of section 3 of the act of February 28, 1891 (26 Stat. 783), as amended May 29, 1924 (43 Stat. 244), leases for oil, gas, and other minerals may be made with the consent of the tribal council on treaty reservations in all States. Section 16 of the Indian Reorganization Act, approved June 18, 1934 (48 Stat. 934), provides that organized Indian tribes shall have the power to prevent the leasing of tribal lands. Under section 17 of that act Indian tribes to which charters of incorporation issue are empowered to lease their lands for periods of not more than 10 years. There is at present no law under which Executive order lands may be leased for mining, outside of the States mentioned in the act of June 30, 1919, except for oil and gas mining purposes, unless the tribes are hereafter qualified under sections 16 and 17 of the Indian Reorganization Act. One of the purposes of the legislation now proposed, therefore, is to obtain uniformity so far as practicable of the law relating to the leasing of tribal lands for mining purposes.

The act of June 30, 1919, requires the formal opening of lands for prospecting, location, and lease, by the Secretary of the Interior, before an application for a lease for minerals other than oil and gas can be considered. It also requires that a person desiring to lease shall locate the mining claims as under the United States mining laws, file formal location notice; and under the regulations he must have the lands surveyed if they have not already been surveyed, all in according with the mining laws applicable to the public domain. This frequently results in long delay and is often quite an expense to an applicant for a lease. Frequently we have requests for leases for the purpose of removing sand and gravel for road-grading

purposes, or for the quarrying of stone, either for building or grading purposes in connection with which there would be little or no under-surface workings. In such cases, applicants for leases are required to go through all the formality and expense necessary to acquiring actual mining leases. Sometimes the time and expense of making the locations and of having the land surveyed are more than they care to undertake although the material desired may be very conveniently located and could be profitably utilized; and consequently the opportunity to lease the land is lost, and the revenue, while perhaps not a great deal in a particular instance would amount to considerable in such cases through the entire Indian Service.

Section 26 of the act of June 30, 1919, *supra*, as amended by the acts of March 3, 1921 (41 Stat. 1231) and December 16, 1926 (44 Stat. 922-923), places unallotted Indian lands within the States mentioned therein upon the same basis for prospecting and leasing for metalliferous minerals as lands of the public domain, after such Indian reservation lands have been declared opened by the Secretary of the Interior. It has been held that the Secretary of the Interior has no discretion under the said section in the matter of granting a lease to an applicant who has properly located his claim and complied with the laws and regulations of the Department thereunder; and in several instances it has been necessary to grant the lease, notwithstanding the fact that the Indians of the reservation were opposed to leasing the lands. In other words, under that law, neither this Department nor the Indian Tribal Council is in a position to prevent the acquisition of a lease after the lands have been declared open to prospecting and lease, and the Indians at no time have any voice in the granting of such leases.

It is not believed that the present law is adequate to give the Indians the greatest return from their property. As stated, present law provides for locating and taking mineral leases in the same manner as mining locations

are made on the public lands of the United States; but there are disadvantages in following this procedure on Indian lands that are not present in applying for a claim on the public domain. For instance, on the public domain the discoverer of a mineral deposit gets extralateral rights and can follow the ore beyond the side lines indefinitely, while on the Indian lands under the act of June 30, 1919, he is limited to the confines of the survey markers not to exceed 600 feet by 1,300 feet in any one claim. The draft of the bill herewith would permit the obtaining of sufficient acreage to remove the necessity of extralateral rights with all its attending controversies.

The most urgent change is in the interest of leasing deposits of building stone, sand, gravel, and metalliferous minerals. For instance, the well-known iron deposit on the Fort Apache Indian Reservation, outcropping along the canyon wall for a distance of about 2 miles and 20 feet thick, with an estimated ore reserve of over 15 million tons, now must be "discovered" and located and monumented and then an application made for a lease. Under the present law only the outcrop along the canyon wall can be taken up under the lease as there are no outcrops of iron ore back from the face of the cliff. This deposit, it is believed, could be leased to better advantage at public auction and in definite areas rather than to anyone who erects a few monuments along the outcrop and applies for a preference right to a lease, through tying up the land with a long strip 600 feet wide. This deposit of iron ore is about 30 miles from a railroad, and anyone interested and considering building a railroad and developing the property would want a reserve greater than 600 feet back from the edge of the cliff. This deposit should appropriately be laid out in blocks extending at least 1 mile back from the outcrop.

Coal deposits on the several reservations are not adaptable to the discovery and location feature of the present act which has very limited application. The presence of

coal is usually known by geological association, and leases may be made with reasonable assurance before any coal is actually exposed on the land. Deposits or marl along the west side of Pyramid Lake, Nev., can be seen for a distance of many miles, yet they must be discovered and located in accordance with the provisions of law relating to placer mining claims and leased to the person who erects monuments thereon. Deposits of sand, gravel, and building stone are now similarly leased, even though the deposits are well known and could be leased with greater advantage to the Indians in definite areas.

The attached draft of bill, it is believed, would be a more satisfactory law for the leasing of Indian lands for general mining purposes. It will bring all mineral-leasing matters in harmony with the Indian Reorganization Act, and I recommend that it be enacted.

The Acting Director of the Bureau of the Budget has advised that there is no objection to the presentation of this report to the Congress.

Sincerely yours,

CHARLES WEST,
Acting Secretary of the Interior.

APPENDIX K

25 CFR Ch. 1 (4-1-85 Edition)

Bureau of Indian Affair, Interior

SUBCHAPTER I—ENERGY AND MINERALS

PART 211—LEASING OF TRIBAL LANDS FOR MINING

AUTHORITY: Secs. 16, 17, 48 Stat. 987, 988, sec. 9, 49 Stat. 1968, sec. 4, 52 Stat. 348; 25 U.S.C. 396d, 476, 477, 509. Interpret or apply secs. 1, 2, 49 Stat. 1250; 48 U.S.C. 358a, 362, unless otherwise noted.

SOURCE: 22 FR 10588, Dec. 24, 1957, unless otherwise noted. Redesignated at 47 FR 13327, Mar. 30, 1982.

§ 211.1 Definitions.

(a) The term "superintendent" in this part refers to the superintendent or other officer of the Bureau of Indian Affairs or of the Government who may have jurisdiction over the lands involved.

(b) The term "supervisor" in this part refers to a representative of the Secretary of the Interior, under direction of the United States Geological Survey, authorized and empowered to supervise and direct operations under oil and gas or other mining leases, to furnish scientific and technical information and advice, to ascertain and record the amount and value of production, and to determine and record rentals and royalties due and paid.

CROSS REFERENCE: For rules and regulations of the Geological Survey, see 30 CFR Chapter II.

HOW TO ACQUIRE LEASES

§ 211.1a Existing permits or leases on minerals acquired for the Ute Indian Tribe of the Uintah and Ouray Reservation, Utah, and the Pueblos of Zia and Jemez, New Mexico.

By the Act of July 14, 1956 (70 Stat. 546), title to the minerals underlying certain lands in Utah was vested

in the United States in trust for the Ute Indian Tribe of the Uintah and Ouray Reservation and by the Act of August 2, 1956 (70 Stat. 941), title to certain land in New Mexico and the improvements thereon was declared to be in the United States of America in trust for the Pueblos of Zia and Jemez, subject to valid and existing rights. Existing mineral prospecting permits and mining leases on these lands issued pursuant to 43 CFR and all action on the permits and leases shall be administered by the Secretary of the Interior or his authorized representative in accordance with the regulations set forth in Title 43 of the Code of Federal Regulations, except as follows:

(a) Appeals from administrative action shall be made pursuant to applicable regulations set forth in this title.

(b) Payments or reports required by the leases, permits, or regulations in 43 CFR shall be made to the Superintendent having jurisdiction over the land involved instead of the officer of the Bureau of Land Management designated in Title 43 of the Code of Federal Regulations.

[25 FR 12408, Dec. 3, 1960. Redesignated at 47 FR 13327, Mar. 30, 1982]

§ 211.2 Lands to be made by tribes.

Indian tribes, bands or groups may, with the approval of the Secretary of the Interior or his authorized representative, lease their land for mining purposes. No oil and gas lease shall be approved unless it has first been offered at an advertised sale in accordance with § 211.3. Leases for minerals other than oil and gas shall be advertised for bids as prescribed in § 211.3 unless the Commissioner grants to the Indian owners written permission to negotiate for a lease. Negotiated leases, accompanied by proper bond and other supporting papers, shall be filed with the Superintendent of the appropriate Indian Agency within 30 days after such permission shall have been granted by the Commissioner to negotiate the lease. The appropriate Area Director is authorized in proper cases to grant a reasonable extension of this period prior

to its expiration. The right is reserved to the Secretary of the Interior to direct that negotiated leases be rejected and that they be advertised for bids. All leases shall be approved by the Secretary of the Interior or his duly authorized representative.

[23 FR 9393, Dec. 4, 1958. Redesignated at 47 FR 13327, Mar. 30, 1982]

§ 211.3 Sale of oil and gas leases.

(a) At such times and in such manner as he may deem appropriate, after being authorized by the tribal council or other authorized representative of the tribe, the superintendent shall publish notices at least thirty days prior to the sale, unless a shorter period is authorized by the Commissioner of Indian Affairs, that oil and gas leases on specific tracts, each of which shall be in a reasonably compact body, will be offered to the highest responsible bidder for a bonus consideration, in addition to stipulated rentals and royalties. Each bid must be accompanied by a cashier's check, certified check or postal money order, payable to the payee designated in the invitation to bid, in an amount not less than 25 percent of the bonus bid. Within 30 days after notification of being the successful bidder, said bidder must remit the balance of the bonus, the first year's rental, and his share of the advertising costs, and shall file with the superintendent the lease in completed form. The superintendent may, for good and sufficient reasons, extend the time for the completion and submission of the lease form, but no extension shall be granted for remitting the balance of moneys due. If the successful bidder fails to pay the full consideration within said period, or fails to file the completed lease within said period or extension thereof, or if the lease is disapproved through no fault of the lessor or the Department of the Interior, 25 percent of the bonus bid will be forfeited for the use and benefit of the Indian lessor.

(b) All notices or advertisements of sales of oil and gas leases shall reserve to the Secretary of the Interior the right to reject all bids when in his judgment the in-

terests of the Indians will be best served by so doing, and that if no satisfactory bid is received, or if the accepted bidder fails to complete the lease, or if the Secretary of the Interior shall determine that it is unwise in the interests of the Indians to accept the highest bid, the Secretary may readvertise such lease for sale, or if deemed advisable, with the consent of the tribal counsel or other governing tribal authorities, a lease may be made by private negotiations. The successful bidder or bidders will be required to pay his or their share of the advertising costs. Amounts received from unsuccessful bidders will be returned; but when no bid is accepted on a tract, the costs of advertising will be assessed against the applicant who requested that said tract be advertised.

[22 FR 10588, Dec. 24, 1957, as amended at 23 FR 7068, Sept. 12, 1958. Redesignated at 47 FR 13327, Mar. 30, 1982]

§ 211.3a Leases for subsurface storage of oil or gas.

(a) The Secretary of the Interior, or his authorized representative, may approve, subject to obtaining the prior consent of the Indian owners, storage leases, or modifications, amendments, or extensions of oil and gas or other mining leases, on tribal lands subject to lease under the Act of May 11, 1938 (52 Stat. 347; 25 U.S.C. 396a), and on allotted lands subject to lease under the Act of March 3, 1909 (35 Stat. 783; 25 U.S.C. 396), to provide for the subsurface storage of oil or gas irrespective of the lands from which production is initially obtained. The storage lease, or modification, amendment, or extension, shall provide for the payment of such storage fee or rental on such oil or gas as may be determined adequate in each case, or, in lieu thereof, for a royalty other than that prescribed in the oil and gas lease when such stored oil and gas is produced in conjunction with oil or gas not previously produced.

(b) The Secretary of the Interior or his authorized representative may approve, subject to obtaining the prior

consent of the Indian owners, a provision in an oil and gas lease, under which storage of oil and gas is authorized, for continuance of the lease at least for the period of such storage use and so long thereafter as oil or gas not previously produced is produced in paying quantities.

(c) Applications for subsurface storage of oil or gas shall be filed in triplicate with the oil and gas supervisor and shall disclose the ownership of the lands involved, the parties in interest, the storage fee, rental, or royalty offered to be paid for such storage, and all essential information showing the necessity for such project. Enough copies of the final agreement signed by the Indian owners and other parties in interest shall be submitted for the approval of the Secretary, or his authorized representative, to permit retention of five copies by the Department after approval.

[25 FR 9836, Oct. 14, 1960. Redesignated at 47 FR 13327, Mar. 30, 1982]

§ 211.4 Government employees cannot acquire leases.

No lease, assignment thereof, or interest therein will be approved to any employee or employees of the United States Government whether connected with the Bureau of Indian Affairs or otherwise, and no employee of the Interior Department shall be permitted to acquire any interest in any mineral lease covering restricted Indian lands by ownership of stock in corporations having such leases or in any other manner.

(R.S. 2078; 25 U.S.C. 68)

§ 211.5 Corporations and corporate information.

If the applicant for a lease is a corporation, it shall file evidence of authority of its officers to execute papers; and with its first application it shall also file a certified copy of its articles of incorporation, and, if foreign to

the State in which the lands are located, evidence showing compliance with the corporation laws thereof. Statements of changes in officers and stockholders shall be furnished by a corporation lessee to the superintendent January 1 of each year, and at such other times as may be requested. Whenever deemed advisable in any case the superintendent may require a corporation applicant or lessee to file:

(a) Lists of officers, principal stockholders, and directors, with post-office addresses and number of shares held by each.

(b) A sworn statement of the proper officer showing:

(1) The total number of shares of the capital stock actually issued and the amount of cash paid into the treasury on each share sold; or, if paid in property, the kind, quantity, and value of the same paid per share.

(2) Of the stock sold, how much remains unpaid and subject to assessment.

(3) The amount of cash the company has in its treasury and elsewhere.

(4) The property, exclusive of cash, owned by the company and its value.

(5) The total indebtedness of the company and the nature of its obligations.

(6) Whether the applicant or any person controlling, controlled by or under common control with the applicant has filed any registration statement, application for registration, prospectus or offering sheet with the Securities and Exchange Commission pursuant to the Securities Act of 1933 or the Securities Exchange Act of 1934 or said Commission's rules and regulations under said acts; if so, under what provisions of said acts or rules and regulations; and what disposition of any such statement, application, prospectus or offering sheet has been made.

(c) Affidavits of individual stockholders, setting forth in what corporations or with what persons, firms, or associations such individual stockholders are interested in mining leases on restricted lands within the State, and whether they hold such interests for themselves or in trust.

CROSS REFERENCE: For rules and regulations of the Securities and Exchange Commission, see 17 CFR Chapter II.

§ 211.6 Bonds.

(a) Lessee shall furnish with each lease a bond (Form 5-154b), and an assignee of a lease shall furnish with each assignment a bond (Form 5-154m), with an acceptable company authorized to act as sole surety, or with two or more personal sureties and a deposit as collateral security of any public-debt obligations of the United States guaranteed as to principal and interest by the United States, equal to the full amount of such bonds, or other collateral satisfactory to the Secretary of the Interior, or show ownership of unencumbered real estate of the value equal to twice the amount of the bonds. Lessee may file a bond on Form 5-154a without sureties and a deposit as collateral security of Government bonds equal in value to the full amount of the bond. Lease bonds shall not be less than the following amounts:

For less than 80 acres	$1,000
For 80 acres and less than 120 acres	1,500
For 120 acres and not more than 160 acres	2,000
For each additional 40 acres, or part thereof, above 160 acres	500

Provided, That for leases for minerals other than oil and gas the Secretary of the Interior or his authorized representative with the consent of the Indian landowner may authorize a bond for a lesser amount if, in his opinion, the circumstances warrant and the interests of the

Indian landowners are fully protected: *Provided further,* That a lessee may file one bond (Form 5-154f), in the sum of $15,000 for all leases of minerals, in any one State and which may also include leases on that part of an Indian reservation extending into State contiguous thereto, to which the lessee may become a party: *And provided further,* That the total acreage covered by the bond shall not exceed 10,240 acres.

(b) In lieu of the bonds required under paragraph (a) of this section, a lessee may furnish a bond (Form 5-156) in the sum of $75,000 for full nationwide coverage with an acceptable company authorized to act as sole surety to cover all oil and gas leases and oil and gas prospecting permits without geographic or acreage limitation to which the lessee or permittee is or may become a party.

(c) The right is specifically reserved to increase the amount of bonds and the collateral security prescribed in paragraph (a) of this section in any particular case when the officer in charge deems it proper to do so. The nationwide bond may be increased at any time in the discretion of the Secretary of the Interior.

[22 FR 10588, Dec. 24, 1957, as amended at 26 FR 164, Jan. 10, 1961. Redesignated at 47 FR 13327, Mar. 30, 1982]

§ 211.7 Lessees to furnish additional information.

The superintendent may, either before or after approval of a lease, call for any additional information desired to carry out the regulations in this part. If a lessee shall fail to furnish the papers necessary to put his lease and bond in proper form for consideration, the superintendent shall forward such lease for disapproval.

§ 211.8 Lands to be in compact body.

The area covered by a lease shall be in a reasonably compact body and shall conform to the system of public-

land surveys, except that leases covering lode ground may consist of one or more adjoining parallelograms 1,500 feet in length by 600 feet in width, as provided by the United States mining laws. No lease under the regulations in this part shall convey any extralateral rights, and no coal lease shall have a length exceeding 1 mile along the outcrop.

§ 211.9 Acreage limitation.

A lessee may acquire more than one lease but no single lease shall be granted for mining purposes on Indian tribal or restricted Indian lands, exclusive of Osage and Quapaw lands, in excess of the following acreage except where the rule of approximation applies:

(a) For oil and gas and all other minerals, except coal, 2,560 acres.

(b) (1) For coal, a lease shall ordinarily be limited to 2,560 acres. The Commissioner may, however, upon application, approve the combining of leases held by one or more lessees, or approve the issuance of a single lease for more than 2,560 acres in a reasonably compact form, if he shall find that the approval of such larger acreage is in the interest of the lessor and is necessary to permit the establishment or construction of thermal electric power plants or other industrial facilities on or near the reservation. He may prescribe provisions in such larger leases to require relinquishment of acreage in the event of failure to construct facilities, or may require advance rental or minimum royalty payments on a part of the acreage as a condition for combining leases or issuance of a single lease in excess of 2,560 acres.

(2) The Commissioner, with the consent of the lessor, may alter, change, or modify the development and producing requirements of the several leases and provide that operations and production on one lease shall be deemed to satisfy the development and producing requirements as to each lease combined.

§ 211.10 Term of leases.

Mining leases may be made for a specified term not to exceed ten years from the date of approval by the Secretary of the Interior, or his authorized representative, and as much longer as the substances specified in the lease are produced in paying quantities.

§ 211.11 Government reserves right to buy minerals produced.

In time of war or other public emergency all of the executive departments of the United States Government shall have the option to purchase at the posted market price on the date of sale all or any part of the substance or substances produced under any lease.

RENTS AND ROYALTIES

§ 211.12 Manner of payments.

(a) Except where otherwise provided by the terms of leases where the tribes are organized under the act of June 18, 1934 (48 Stat. 984; 25 U.S.C. 461-479), all rents and other payments due under leases which have been or may be approved by the Secretary of the Interior shall be paid to the superintendent or to such other person as may be designated by the Secretary of the Interior, for the benefit of the lessors. Except advance payments for the first year which shall be sent direct to the superintendent at the time of filing leases, payments of rental and royalty under leases shall be transmitted through the supervisor, shall be accompanied by a statement by the lessee, in triplicate, showing the specific items of rental or royalty that the remittance is intended to cover, and shall be made at such time or times as the lease provides.

(b) In the event of the discovery of minerals in paying quantities all advance payments shall be allowed as

credit on stipulated royalties for the year for which such advance payments have been made. No refund will be made under oil, gas, or other mining leases, in the event that royalty from production is not sufficient to equal the advance payment, nor will any part of the moneys so paid be refunded to the lessee because of any subsequent surrender or cancellation of the lease, nor shall the lessee be relieved from the obligation to pay said advance rental annually when it becomes due, by reason of any subsequent surrender or cancellation of the lease.

§ 211.13 Rates of rentals and royalties under oil and gas leases.

(a) The lessee shall pay, beginning with the date of approval of oil and gas leases by the Secretary of the Interior, a rental of $1.25 per acre per annum in advance during the continuance thereof, together with a royalty of 12½ percent of the value or amount of all oil, gas, and/or natural gasoline, and/or all other hydrocarbon substances produced and saved from the land leased, save and except oil, and/or gas used by the lessee for development and operation purposes on the lease, which oil or gas shall be royalty free. A higher rate of royalty may be fixed by the Secretary of the Interior or his authorized representative, prior to the advertisement of land for oil and gas leases. During the period of supervision, "value" for the purposes of the lease may, in the discretion of the Secretary of the Interior, be calculated on the basis of the highest price paid or offered (whether calculated on the basis of short or actual volume) at the time of production for the major portion of the oil of the same gravity, and gas, and/or natural gasoline, and/or all other hydrocarbon substances produced and sold from the field where the leased lands are situated, and the actual volume of the marketable product less the content of foreign substances as determined

by the supervisor. The actual amount realized by the lessee from the sale of said products may, in the discretion of the Secretary of the Interior, be deemed mere evidence of or conclusive evidence of such value. When paid in value, such royalties shall be due and payable monthly on the last day of the calendar month following the calendar month in which produced; when royalty on oil produced is paid in kind, such royalty oil shall be delivered in tanks provided by the lessee on the premises where produced without cost to the lessor unless otherwise agreed to by the parties thereto, at such time as may be required by the lessor. The lessee shall not be required to hold such royalty oil in storage longer than 30 days after the end of the calendar month in which said oil is produced. The lessee shall be in no manner responsible or held liable for loss or destruction of such oil in storage by causes beyond the lessee's control. In determining the value for royalty purposes of products, such as natural gasoline, that are derived from treatment of gas, a reasonable allowance for the cost of manufacture shall be made, such allowance to be two-thirds of the value of the marketable product unless otherwise determined by the Secretary of the Interior on application of the lessee or on his own initiative, and that royalty will be computed on the value of gas or casinghead gas, or on the products thereof (such as residue gas, natural gasoline, propane, butane, etc.), whichever is the greater.

(b) If the leased premises produce gas in excess of the lessee's requirements for the development and operation of said premises, then the lessor may use sufficient gas, free of charge, for any desired school or other buildings belonging to the tribe, by making his own connections to a regulator installed, connected to the well and maintained by the lessee, and the lessee shall not be required to pay royalty on gas so used. The use of such gas shall be at the lessor's risk at all times.

§ 211.14 Annual rentals and expenditures for development on leases other than oil and gas.

(a) Unless otherwise authorized by the Secretary or his authorized representative (1) a lease for minerals other than oil and gas shall provide for a yearly development expenditure of not less than $10 per acre and (2) all such leases shall provide for a rental payment of not less than $1 for each acre or fraction of an acre payable on or before the first day of each lease year.

(b) Within 20 days after the lease year, an itemized statement, in duplicate, of the expenditure for development under a lease for minerals other than oil and gas shall be filed with the Superintendent. The lessee must certify the statement under oath.

§ 211.14a Suspension of operations and production on leases for minerals other than oil and gas.

The Secretary of the Interior or his authorized representative, after obtaining the consent of the tribe, may authorize suspension of operating and producing requirements on mining leases for minerals other than oil and gas whenever during the primary term of the leases, it is considered that marketing facilities are inadequate or economic conditions unsatisfactory. Applications by lessees for relief from all operating and producing requirements on such mineral leases shall be filed in triplicate, in the office of the Regional Mining Supervisor of the Geological Survey and a copy thereof filed with the Superintendent. Complete information must be furnished showing the necessity for such relief. Suspension of operations and production shall not relieve the lessee from the obligations of continued payment of the annual rental or the minimum royalty.

[24 FR 9510, Nov. 26, 1959. Redesignated at 47 FR 13327, Mar. 30, 1982]

§ 211.15 Royalty rates for minerals other than oil and gas.

Unless otherwise authorized by the Commissioner of Indian Affairs, the minimum rates for minerals other than oil and gas shall be as follows:

(a) For substances other than gold, silver, copper, lead, zinc, tungsten, coal, asphaltum and allied substances, oil, and gas, the lessee shall pay quarterly or as otherwise provided in the lease, a royalty of not less than 10 percent of the value, at the nearest shipping point, of all ores, metals, or minerals marketed.

(b) For gold and silver the lessee shall pay quarterly or as otherwise provided in the lease, a royalty of not less than 10 percent to be computed on the value of bullion as shown by mint returns after deducting forwarding charges to the point of sale; and for copper, lead, zinc, and tungsten, a royalty of not less than 10 percent to be computed on the value of ores and concentrates as shown by reduction returns after deducting freight charges to the point of sale. Duplicate returns shall be filed by the lessee with the Superintendent within 10 days after the ending of the quarter or other period specified in the lease within which such returns are made: *Provided, however,* That the lessee shall pay a royalty of not less than 10 percent of the value of the ore or concentrates sold at the mine unless otherwise provided in the lease.

(c) For coal the lessee shall pay quarterly or as otherwise provided in the lease, a royalty of not less than 10 cents per ton of 2,000 pounds of mine run, or coal as taken from the mine, including what is commonly called "slack".

(d) For asphaltum and allied substances the lessee shall pay quarterly or as otherwise provided in the lease, a royalty of not less than 10 cents per ton of 2,000 pounds

on crude material or not less than 60 cents per ton on refined substances.

§ 211.16 Time of making royalty payments.

Royalty payments under producing oil and gas leases shall be made monthly on or before the last day of the calendar month following the calendar month for which such payment is to be made.

§ 211.17 Division orders.

(a) Lessees may make arrangements with the purchasers of oil for the payment of the royalties to the superintendent by such purchasers, but such arrangement, if made, shall not operate to relieve a lessee from responsibility should the purchaser fail or refuse to pay royalties when due. Where lessees avail themselves of this privilege, division orders permitting the pipe line companies or other purchasers of the oil to withhold the royalty interest shall be executed and forwarded to the supervisor for approval, as pipe line companies are not permitted to accept or run oil from leased Indian lands until after the approval of a division order showing that the lessee has a lease regularly approved and in effect. When the lessee company runs its own oil, it shall execute an intracompany division order and forward it to the supervisor for his consideration. The right is reserved for the supervisor to cancel a division order at any time or require the pipe line company to discontinue to run the oil of any lessee who fails to operate the lease properly or otherwise violates the provisions of the lease, or the regulations in this part, or of the operating regulations.

(b) When oil is taken by authority of a division order, the lessee or his representative shall be actually present when the oil is gauged and records are made of the temperature, gravity, and impurities. The lessee will be held responsible for the correctness and the correct recording and reporting of all of the foregoing measurements;

which, except lowest gauge, shall be made at the time the oil is turned into the pipe line. Failure of the lessee to perform properly these duties will subject the division order to revocation.

CROSS REFERENCE: For oil and gas operating regulations of the Geological Survey, see 30 CFR Part 221.

§ 211.18 Inspection of premises, books and accounts.

Lessees shall agree to allow the lessors and their agents or any authorized representative of the Interior Department to enter, from time to time, upon and into all parts of the leased premises for the purpose of inspection, and shall further agree to keep a full and correct account of all operations and make reports thereof, as required by the regulations of the Department governing operations on public and restricted Indian lands; and their books and records, showing manner of operations and persons interested, shall be open at all times for examination of such officers of the Department as shall be instructed in writing by the Secretary of the Interior or authorized by regulations to make such examination.

§ 211.19 Diligence and prevention of waste.

The lessee shall exercise diligence in drilling and operating wells for oil and gas on the leased lands while such products can be secured in paying quantities; carry on all operations in a good and workmanlike manner in accordance with approved methods and practice, having due regard for the prevention of waste of oil or gas developed on the land, or the entrance of water through wells drilled by the lessee to the productive sands or oil or gas-bearing strata to the destruction or injury of the oil or gas deposits, the preservation and conservation of the property for future productive operations, and to the health and safety of workmen and employees; plug securely all wells before abandoning the same and to shut

off effectually all water from the oil or gas-bearing strata; not drill any well within 200 feet of any house or barn on the premises without the lessor's written consent approved by the superintendent; carry out at his expense all reasonable orders and requirements of the supervisor relative to prevention of waste, and preservation of the property and the health and safety of workmen; bury all pipelines crossing tillable lands below plow depth unless other arrangements therefor are made with the superintendent; pay the lessor all damages to crops, buildings, and other improvements of the lessor occasioned by the lessee's operation: *Provided*, That the lessee shall not be held responsible for delays or casualties occasioned by causes beyond the lessee's control.

§ 211.20 Permission to start operations.

(a) No operations will be permitted on any lease before it is approved by the Secretary of the Interior.

(b) Written permission must be secured from the supervisor before any operations are started on the leased premises. After such permission is secured the operations must be in accordance with the operating regulations promulgated by the Secretary of the Interior. Copies of the regulations in this part may be secured from either the supervisor or the superintendent and no operations shall be attempted without a study of the operating regulations.

§ 211.21 Restrictions on operations.

(a) Oil and gas leases issued under the provisions of the regulations in this part shall be subject to imposition by the Secretary of the Interior of such restrictions as to time or times for the drilling of wells and as to the production from any well or wells as in his judgment may be necessary or proper for the protection of the natural resources of the leased land and in the interest of the lessor. In the exercise of his judgment the Secretary of the

Interior may take into consideration, among other things, the Federal laws, State laws, regulations by competent Federal or State authorities, lawful agreements among operators regulating either drilling or production or both, and any regulatory action desired by tribal authorities.

(b) All such leases shall be subject to any cooperative or unit development plan affecting the leased lands that may be required by the Secretary of the Interior, but no lease shall be included in any cooperative or unit plan without prior approval of the Secretary of the Interior and consent of the Indian tribe affected.

§ 211.22 Penalties.

Failure of the lessee to comply with any provisions of the lease, of the operating regulations, of the regulations in this part, order of the superintendent or his representative, or of the orders of the supervisor or his representative, shall subject the lease to cancellation by the Secretary of the Interior or the lessee to a penalty of not more than $500 per day for each and every day the terms of the lease, the regulations, or such orders are violated; or to both such penalty and cancellation: *Provided*, That the lessee shall be entitled to notice and hearing, within 30 days after such notice, with respect to the terms of the lease, regulations, or orders violated, which hearing shall be held by the supervisor, whose findings shall be conclusive unless an appeal be taken to the Secretary of the Interior within 30 days after notice of the supervisor's decision, and the decision of the Secretary of the Interior upon appeal shall be conclusive.

§ 211.23 Mines to be timbered properly.

In mining operations the lessee shall keep the mine well and sufficiently timbered at all points where necessary, in accordance with good mining practice, and in such manner as may be necessary to the proper preservation of the leased property and safety of the workmen.

§ 211.24 Surrender of leased premises in good condition.

On expiration of the term of a lease, or when a lease is surrendered, the lessee shall deliver to the Government the leased ground with the mine workings in good order and condition, and bondsmen will be held for such delivery in good order and condition, unless relieved by the Secretary of the Interior for cause. It shall, however, be stipulated that the machinery necessary to operate the mine is the property of the lessee, but that it may be removed by him only after the condition of the property has been ascertained by inspection by the Secretary of the Interior or his authorized agents, to be in satisfactory condition.

§ 211.25 Fees.

Unless otherwise authorized by the Secretary of the Interior or his authorized representative, each lease, mining permit, sublease, or assignment shall be accompanied at the time of filing by a fee of $10. Such fee will not be required on sand and gravel permits issued to States, counties, or other municipal bodies.

(Sec. 1, 41 Stat. 415, as amended: 25 U.S.C. 413)

[24 FR 7949, Oct. 2, 1959. Redesignated at 47 FR 13327, Mar. 30, 1982]

§ 211.26 Assignments and overriding royalties.

(a) Approved leases or any interest therein may be assigned or transferred only with the approval of the Secretary of the Interior, and to procure such approval the assignee must be qualified to hold such lease under existing rules and regulations and shall furnish a satisfactory bond conditioned for the faithful performance of the covenants and conditions thereof: *Provided,* That in order for such assignment to receive favorable consideration the lessee shall assign either his whole interest or an undivided interest in the whole lease.

(b) No lease or interest therein or the use of such lease shall be assigned, sublet, or transferred, directly or indirectly by working or drilling contract, or otherwise, without the consent of the Secretary of the Interior.

(c) Assignments of leases, and stipulations modifying the terms of existing leases, which stipulations are also subject to the approval of the Secretary of the Interior, shall be filed with the superintendent within 30 days after the date of execution.

(d) Agreements creating overriding royalties or payments out of production on oil and gas leases shall not be considered as interests in the leases as such term is used in this section. Agreements creating overriding royalties or payments out of production are hereby authorized and the approval of the Department of the Interior or any agency thereof shall not be required with respect thereto, but such agreements shall be subject to the condition that nothing in any such agreement shall be construed as modifying any of the obligations of the lessee, including, but not limited to, obligations for diligent development and operation, protection against drainage, compliance with oil and gas operating regulations (30 CFR Part 221), and the requirement for departmental approval before abandonment of any well. All such obligations are to remain in full force and effect, the same as if free of any such royalties or payments. The existence of agreements creating overriding royalties or payments out of production, whether or not actually paid, shall not be considered as justification for the approval of abandonment of any well. Nothing in this paragraph revokes the requirement for approval of assignments and other instruments which is required in this section, but any overriding royalties or payments out of production created by the terms of such assignments or instruments shall be subject to the condition stated above. Agreements creating overriding royalties or payments out of production need not be filed with

the Superintendent unless incorporated in assignments or instruments required to be filed pursuant to this section.

[22 FR 10588, Dec. 24, 1957, as amended at 23 FR 9738, Dec. 18, 1958. Redesignated at 47 FR 13327, Mar. 30 1982]

§ 211.27 Cancellation.

(a) When, in the opinion of the Secretary of the Interior, the lessee has violated any of the terms and conditions of a lease or of the applicable regulations, the Secretary of the Interior shall have the right at any time after 30 days' notice to the lessee specifying the terms and conditions violated, and after a hearing, if the lessee shall so request within 30 days after issuance of the notice, to declare such lease null and void, and the lessor shall then be entitled and authorized to take immediate possession of the land.

(b) On the following conditions, the lessee may, on approval of the Secretary of the Interior, surrender a lease or any part of it:

(1) That he make application for cancellation to the superintendent having jurisdiction over the land.

(2) That he pay a surrender fee of $1 at the time the application is made.

(3) That he pay all royalties and rentals due to the date of such application.

(4) That he make a satisfactory showing that full provision has been made for conservation and protection of the property and that all wells, drilled on the portion of the lease surrendered, have been properly abandoned.

(5) If the lease has been recorded, that he file, with his application, a recorded release of the acreage covered by the application.

(6) If the application is for the cancellation of the entire lease or the entire undivided portion, that he surrender the lease: *Provided,* That where the application is made by an assignee to whom no copy of the lease was delivered, he will be required to surrender only his copy of the assignment.

(7) If the lease (or portion being surrendered or canceled) is owned in undivided interests by more than one party, then all parties shall join in the application for cancellation.

(8) That all required fees and papers must be in the mail or received on or before the date upon which rents and royalties become due, in order for the lessee and his surety to be relieved from liability for the payment of such royalties and rentals.

(9) If there has been a contest respecting a lease or leases, the approved, the disapproved, or the cancelled parts thereof will be held in the office of the superintendent for 5 days after the Department's decision has been promulgated, by mail or delivery, and will not be delivered, if within that period a motion for review and reconsideration be filed, until such motion is passed upon by the Department.

(10) In the event oil or gas is being drained from the leased premises by wells not covered by a lease; the lease, or any part of it, may be surrendered, only on such terms and conditions as the Secretary of the Interior may determine to be reasonable and equitable.

(c) No part of any advance rental shall be refunded to the lessee nor shall he be relieved, by reason of any subsequent surrender or cancellation of the lease, from the obligation to pay said advance rental when it becomes due.

§ 211.27a Prospecting permits.

With the consent of the tribal authorities the superintendent may issue permits to prospect for minerals

other than oil and gas upon tribal lands. Such permits must describe the area to be prospected and definitely state the period of time within which such work is permitted. No ores shall be removed from the reservation under such permits, except samples for assay and experimental purposes. A prospecting permit will not give the permittee any preference right to a lease, unless specifically so stated in the permit, and all permits granting a preference right to a lease must comply with all the laws and regulations applicable to mineral leases on tribal Indian lands.

§ 211.28 Effective date of regulations.

The regulations in this part shall become effective and in full force from and after the date of approval, and shall be subject to change or alteration at any time by the Secretary of the Interior: *Provided*, That no regulations made after the approval of any lease shall operate to affect the term of the lease, rate of royalty, rental, or acreage unless agreed to by both parties to the lease. All former regulations governing the leasing of tribal lands for mining purposes are superseded by the regulations in this part.

§ 211.29 Exemption of leases made by organized tribes.

The regulations in this part may be superseded by the provisions of any tribal constitution, bylaw or charter issued pursuant to the Indian Reorganization Act of June 18, 1934 (48 Stat. 984; 25 U.S.C. 461-479), the Alaska Act of May 1, 1936 (49 Stat. 1250; 48 U.S.C. 362, 258a), or the Oklahoma Indian Welfare Act of June 26, 1936 (49 Stat. 1967; 25 U.S.C., and Sup., 501-509), or by ordinance, resolution or other action authorized under such constitution, bylaw or charter. The regulations in this part, in so far as they are not so superseded, shall apply to leases made by organized tribes if the validity of the lease depends upon the approval of the Secretary of the Interior.

§ 211.30 Forms.

Leases, assignments, and other instruments shall be on forms prescribed by the Secretary of the Interior or his authorized representative and may be obtained from the superintendent or other officer having jurisdiction over the lands.

[24 FR 7949, Oct. 2, 1959. Redesignated at 47 FR 13327, Mar. 30, 1982]

TITLE 30—MINERAL RESOURCES
(7-1-81 Edition)

CHAPTER II—GEOLOGICAL SURVEY

PART 221—OIL AND GAS OPERATING REGULATIONS

AUTHORITY: Sec. 3, 26 Stat. 795, secs. 18, 14, 27, 28, 32, 41 Stat. 426, 442, as amended, 448, as amended, 449, as amended, 450 sec. 7, 42 Stat. 1450, 43 Stat. 244, sec. 6, 46 Stat. 374, sec. 39, 47 Stat. 798, as amended, sec. 40, 48 Stat. 977, sec. 3, 49 Stat. 679, 50 Stat. 842, as amended, sec. 4, 52 Stat. 348, sec. 10, 61 Stat. 915; 25 U.S.C. 397, 356, 30 U.S.C. 223, 184, 185, 189, 236, 25 U.S.C. 398, 30 U.S.C. 306, 209, 229a, 236a, 221i, 25 U.S.C. 396d, 30 U.S.C. 359.

SOURCE: 7 FR 4132, June 12, 1942, unless otherwise noted.

INTRODUCTION; DEFINITIONS

§ 221.1 Introduction.

The regulations in this part will govern the development and production of deposits of oil, gas, and casinghead or natural gasoline, including propane, butane and other hydrocarbons, and fluids, and lands containing such deposits owned or controlled by the United States, and under jurisdiction of the Secretary by law or administrative arrangement. The regulations in this part shall be administered under the Director of the Geological Survey, except that as to lands within naval petroleum reserves they shall be administered under such official as the Secretary of the Navy shall designate.

§ 221.2 Definitions.

The following terms as used in the regulations in this part shall have the meanings here given:

(a) *Secretary.* The Secretary of the Interior, except where lands in naval petroleum reserves are involved, and in that case the Secretary of the Navy.

(b) *Director.* The Director of the Geological Survey, Washington, D.C., having direction of the enforcement of the regulations in this part.

(c) *Supervisor.* The Area Oil and Gas Supervisor, Conservation Division of the Geological Survey; a representative of the Secretary, subject of the direction and supervisory authority of the Director, the Chief, Conservation Division, Geological Survey, and the appropriate Regional Conservation Manager, Conservation Division, Geological Survey, authorized and empowered to supervise and direct oil and gas operations and to perform other duties prescribed in the regulations in this part, or any subordinate acting under his direction.

NOTE: As used in Part 221 the term "Supervisor" means the appropriate Deputy Conservation Manager, Conservation Division of the Geological Survey, or any subordinate acting under his direction.

(d) *Officer in charge.* The supervisor or such other officer as the Secretary may designate to supervise technical operations for the development and production of oil and gas on restricted Indian lands. Over such lands the officer so designated shall exercise the authority and power and perform the duties of supervisor as provided in the regulations in this part.

(e) *Superintendent.* The superintendent of an Indian agency, or other officer authorized to act in matters of record, law, and collections with respect to oil or gas leases for restricted Indian lands.

(f) *Lease.* An agreement which in consideration of covenants to be observed, grants to a lessee the exclusive right and privilege of developing and producing oil or gas deposits owned by the lessor subject to the regulations in this part.

(g) *Leased lands, leasehold.* Lands and deposits covered by a lease as defined in paragraph (f) of this section.

(h) *Producing lease.* A producing lease is one including land on which there is a producible well, either active or shut in, or land determined by the supervisor to be subject to subsurface drainage.

(i) *Lessor.* The party to a lease who holds title to the leased lands.

(j) *Lessee.* The party authorized by a lease, or approved assignment thereof, to develop and produce oil or gas on the leased lands in accordance with the regulations in this part, including all parties holding such authority by or through him.

(k) *Register.* A representative of the Bureau of Land Management in charge of a District Land Office.

(l) *Operator.* The individual, partnership, firm, or corporation that has control or management of operations on the leased land or a portion thereof. The operator may be a lessee, designated agent of the lessee, or holder of rights under an approved operating agreement.

(m) *Designated operator or agent.* The local representative of the lessee or of the operator; may be the holder of operating rights under an approved operating agreement.

(n) *Waste of oil or gas.* Waste of oil or gas, in addition to its ordinary meaning, shall mean the physical waste of oil or gas, and waste, loss, or dissipation of reservoir energy existent in any deposit containing oil or gas and necessary or useful in obtaining the maximum recovery from such deposit.

(1) Physical waste of oil or gas shall be deemed to include the loss or destruction of oil or gas after recovery thereof such as to prevent proper utilization and beneficial use thereof, and the loss of oil or gas prior to recovery thereof by isolation or entrapment, by migration, by premature release of natural gas from solution in oil,

or in any other manner such as to render impracticable the recovery of such oil or gas.

(2) Waste of reservoir energy shall be deemed to include the failure reasonably to maintain such energy by artificial means and also the dissipation of gas energy, hydrostatic energy, or other natural reservoir energy, at any time at a rate or in a manner which would constitute improvident use of the energy available or result in loss thereof without reasonably adequate recovery of oil.

(o) *Gas.* Any fluid, either combustible or noncombustile, which is produced in a natural state from the earth and which maintains a gaseous or rarefied state at ordinary temperature and pressure conditions.

(p) *Oil, crude oil.* Any liquid hydrocarbon substance which occurs naturally in the earth, including drip gasoline or other natural condensates recovered from gas, without resort to manufacturing process.

[7 FR 4132, June 2, 1942, as amended by 38 FR 10001, Apr. 23, 1973; 45 FR 41410, June 19, 1980]

JURISDICTION AND FUNCTIONS OF SUPERVISOR

§ 221.3 Jurisdiction.

Subject to the supervisory authority of the Secretary and the Director, drilling and producing operations, handling and gaging of oil, and the measurement of gas or other products, determination of royalty liability, receipt and delivery to those entitled thereto of royalty accruing to the lessor and paid in amount of production, determination of amount and manner of payment of damages assessed under authority of the regulations in this part for defaults or noncompliance with duties by the lessee and, in general, all operations subject to the regulations in this part are under the jurisdiction of the supervisor for any area as delineated by the Director. As to producing leases of Indian lands, the officer in charge, and as to lands

within naval petroleum reserves, the supervisor shall determine rental liability, record rentals, royalties, and other payments, and maintain lease accounts. Upon request, the supervisor will advise any person concerning the regulations in this part, and will furnish technical information and advice relative to oil and gas development and operation on lands subject hereto. In the exercise of his jurisdiction, the supervisor shall be subject to the direction and supervisory authority of the Chief, Conservation Division, Geological Survey and the appropriate Regional Conservation Manager, Conservation Division, Geological Survey, each of whom may exercise the jurisdiction of the supervisor.

[38 FR 10001, Apr. 23, 1973]

§ 221.4 General functions.

The supervisor is hereby authorized to require compliance with lease terms, with the regulations in this part, and all other applicable regulations, and with applicable law to the end that all operations shall conform to the best practice and shall be conducted in such manner as to protect the deposits of the leased lands and result in the maximum ultimate recovery of oil, gas, or other products with minimum waste. Inasmuch as conditions in one area may vary widely from conditions in another area, the regulations in this part are general, and detailed procedure hereunder in any particular area is subject to the judgment and discretion of the supervisor, and to any real plan of development that may be adopted pursuant to law. The supervisor may require satisfactory evidence that a lease is in good standing, that the lessee or operator is authorized to conduct operations, and that an acceptable bond has been filed before permitting operations on the leased land.

§ 221.5 Supervision of operations.

The supervisor shall inspect and supervise operations under the regulations in this part: prevent waste, dam-

age to formations or deposits containing oil, gas, or water or to coal measures or other mineral deposits, and injury to life or property; and shall issue instructions necessary, in his judgment, to accomplish these purposes.

§ 221.6 Reports and recommendations.

The supervisor shall make reports to his superior administrative officer as to the general condition of leased lands, and the manner in which operations are being conducted and departmental orders are being obeyed, and submit from time to time information and recommendations for safeguarding and protecting surface property and underlying mineral-bearing formations.

§ 221.7 Reports and notices.

The supervisor shall prescribe the manner and form in which records of all operations, reports, and notices shall be made by lessees and operators.

§ 221.8 Required samples, tests, and surveys.

When deemed necessary or advisable, the supervisor is authorized to require that adequate samples be taken and tests or surveys be made in acceptable manner without cost to the lessor to determine the identity and character of formations; the presence or waste of oil, gas, water, or reservoir energy; the quantity and quality of oil, gas, or water; the amount and direction of deviation of any well from the vertical; formation, casing, tubing, or other pressures; and whether operations are being conducted with due regard to the interests of the lessor.

§ 221.9 Damage to mineral deposits, directional drilling, lease obligations, and abandonment.

The supervisor shall require correction, in a manner to be prescribed or approved by him, of any condition which is causing or is likely to cause damage to any formation containing oil, gas, or water or to coal measures or other mineral deposits, or which is dangerous to

life or property or wasteful of oil, gas, or water; require substantially vertical drilling when necessary to protect interests in other properties; demand drilling in accordance with the terms of the lease or of the regulations in this part; and require plugging and abandonment of any well or wells no longer used or useful in accordance with such plan as may be approved or prescribed by him, and, upon failure to secure compliance with such requirement, perform the work at the expense of the lessee, expending available public funds, and submit such report as may be needed to furnish a basis for appropriate action to obtain reimbursement.

§ 221.10 Well potentials and permissible flow.

The supervisor is authorized to fix the percentage of the potential capacity of any oil or gas well that may be utilized or the permissible production of any such well when, in his opinion, such action is necessary to protect the interests of the lessor, or to conform with proration rules established for the field; and to specify the time and method for determining the potential capacity of such wells.

§ 221.11 Well-spacing and well-casing; technical assistance to lessees.

The supervisor shall approve well-spacing and well-casing programs determined to be necessary for the proper development of the leases and assist and advise lessees in the planning and conduct of tests and experiments for the purpose of increasing the efficiency of operations.

§ 221.12 Production records; rentals, royalties, and payments; drainage and waste.

The supervisor shall compile and maintain records of production and prices and determine royalties accrued, estimate drainage and compute losses to the lessor result-

ing therefrom, and estimate the amount and value of oil, gas, and other products wasted. The supervisor shall render monthly to the lessee or his agent, statements, showing the amount of oil, gas, casing-head or natural gasoline, propane, butane, or other hydrocarbons produced or sold and the amount or value of production accruing to the lessor as royalty from each lease; the loss by drainage or waste and the compensation due to the lessor as reimbursement; and, except as to any disposal of gas that shall have been determined by the Secretary of the Interior to be sanctioned by the laws of the United States and of the State in which it occurs, the amount and full value, computed at a price of not less than 5 cents per 1,000 cubic feet, of all gas wasted by blowing, release, escape into the air, or otherwise. Also, as to producing leases of Indian lands and lands within naval petroleum reserves, the supervisor shall determine rental liability, record rental royalty, and other payments, and maintain lease accounts.

§ 221.13 Division orders, run tickets, sales agreement or contracts.

The supervisor is authorized to approve, subject to such conditions as he shall prescribe, division orders or temporary purchase agreements granting to transportation agencies or purchasers authority to receive products from leased lands in accordance with Government rules and regulation; sign run tickets or other receipts for royalty oil or gas delivered to a representative of the lessor or to the lessor's account; and approve sales agreements and contracts, subject to any conditions, modification, or revocation that may be prescribed on review thereof by the Director.

CROSS REFERENCE: For regulations relating to approval of sales agreements or contracts, see Part 223 of this chapter.

§ 221.14 Suspension of operations and production.

On receipt of an application for suspension of operations or production or for relief from any drilling or producing requirement under a lease, the supervisor shall forward such application, with a report and recommendation, to the appropriate official and, pending action thereon, grant such temporary approval as he may deem warranted in the premises, or reject such application, subject to the right of appeal as provided in Part 290 of this chapter.

[7 FR 4132, June 2, 1942, as amended at 38 FR 10001, Apr. 23, 1973]

§ 221.15 Beginning or resumption of drilling or producing operations.

Where drilling or producing operations have been suspended on a lease, the supervisor may approve in writing notice by the lessee of intention to begin or resume such operations: *Provided,* That whenever it appears from facts adduced by or furnished to him that the interests of the lessor require additional drilling or producing operations, the supervisor may require by notice in writing the beginning or resumption of such operations.

§ 221.16 Enforcement.

The supervisor shall enforce the regulations in this part, and his orders issued pursuant thereto by action provided for in §§ 221.53 and 221.54 whenever, in his judgment, such action is necessary or advisable.

§ 221.17 Appeals action.

The supervisor shall receive and promptly render his decision on any matter presented for reconsideration under the regulations in this part and shall receive and promptly transmit for review all appeals filed pursuant to Part 290 of this chapter.

[38 FR 10001, Apr. 23, 1973]

REQUIREMENTS FOR ALL LESSEES
(INCLUDING DESIGNATED OPERATORS)

§ 221.18 Lease terms, regulations, instructions of supervisor, waste, damage, safety, and bond.

The lessee shall comply with the terms of the lease, and of the regulations in this part and any amendments thereof, and with the written instructions of the supervisor, shall take all reasonable precautions to prevent waste, damage to formations or deposits containing oil, gas, or water or to coal measures or other mineral deposits, and injury to life or property, and before drilling or other operations are started, shall have submitted a satisfactory bond.

§ 221.19 Designated operator (or agent).

(a) In all cases where operations on a lease are not conducted by the record owner, but are to be conducted under authority of an operating agreement, an unapproved assignment, or other arrangement, a "designation of operator" shall be submitted to the supervisor, in a manner and form approved by the supervisor, prior to commencement of operations. If the designation of operator form cannot be obtained from the lessee without undue inconvenience to the operator, the supervisor in his discretion may accept in lieu thereof a valid operating agreement approved by the Secretary. A designation of operator will be accepted as authority of operator or his local representative to fulfill the obligations of the lessee and to sign, as operator, any papers or reports required under the regulations in this part. It will rest in the discretion of the supervisor to determine how a local representative of the operator empowered to act in whole or in part in his stead shall be identified.

(b) If the designated operator shall at any time be incapacitated for duty or absent from his designated

address, the operator or the lessee shall designate in writing a substitute to serve in his stead, and, in the absence of such operator or of notice of the appointment of a substitute, any employee of the lessee who is on the leased lands or the contractor or other person in charge of operations will be considered the agent of the lessee for the service of orders or notices and service in person or by ordinary mail upon any such employee, contractor, or other person will be deemed service upon the operator and the lessee. All changes of address and any termination of the operator's authority shall be immediately reported, in writing, to the supervisor or his representative. In case of such termination or of controversy between the lessee and the designated operator, the operator, if in possession of the leasehold will be required to protect the interests of the lessor.

§ 221.20 Well-location restrictions.

(a) The lessee shall not drill any well within 200 feet of any of the outer boundaries of the leased lands except where necessary to protect those lands against wells on land the title to which is not held by the lessor, and then only on consent first had in writing from the supervisor: *Provided*, That for good cause shown in any particular case, and where not prohibited by law, a lessee may be relieved of such restrictions on written consent of the supervisor. The lessee shall not drill any well within 200 feet of the boundary of any legal subdivision without first submitting adequate reasons therefor and obtaining consent in writing from the supervisor, such consent to be subject to such conditions as may be prescribed by said official.

(b) Lessees of Indian lands shall not drill any well within 200 feet of any house or barn standing on the leased lands without the lessor's written consent, approved by the officer in charge and the superintendent.

§ 221.21 Well-spacing and well-casing program, well operations, required offsets, diligence, compensasation in lieu of drilling.

(a) When required by the supervisor, the lessee shall submit an acceptable well-spacing and well-casing program for the lease or area. Such program must be approved by the supervisor and may be modified from time to time as conditions warrant, with the consent and approval of the supervisor.

(b) The lessee shall not begin to drill, redrill, repair, deepen, plug back, shoot, or plug and abandon any well, make water shut-off or formation test, alter the casing or liner, stimulate production by vacuum, acid, gas, air, water injection, or any other method, change the method of recovering production, or use any formation or well for gas storage or water disposal without first notifying the supervisor of his plan and intention and receiving written approval prior to commencing the contemplated work. The approval by the supervisor of a drilling plan does not constitute a determination or opinion that the lessee will be entitled to an extension of his lease under any extension provisions of the public-land or acquired lands mineral leasing laws if he carries out his plan.

(c) The lessee shall drill diligently and produce continuously from such wells as are necessary to protect the lessor from loss of royalty by reason of drainage, or, in lieu thereof, with the consent of the supervisor, he must pay a sum estimated to reimburse the lessor for such loss of royalty, the sum to be computed monthly by the supervisor.

(d) The lessee, whenever drilling or producing operations are suspended for 24 hours or more, shall close the mouth of the well with a suitable plug or other fittings acceptable to the supervisor.

[7 FR 4132, June 2, 1942, as amended at 31 FR 6415, Apr. 28, 1966]

§ 221.22 Well designations, property boundaries, markers for abandoned wells.

The lessee shall mark each and every derrick or well in a conspicuous place with his name or the name of the operator, the serial number of the lease or the name of the lessor if on Indian land, and the number and location of the well, and shall take all necessary means and precautions to preserve these markings. All abandoned wells shall be marked with a permanent monument, on which shall be shown the number and location of the well, unless this requirement is waived in writing by the supervisor. This monument shall consist of a piece of pipe not less than 4 inches in diameter and not less than 10 feet in length, of which 4 feet shall be above the general ground level, the remainder being embedded in cement. The top of the pipe must be closed with a screw cap, cement plug, or by other approved means.

§ 221.23 Well records and reports, plats and maps, samples, tests, and surveys.

(a) The lessee shall keep on the leased lands or at his headquarters in the field, or otherwise conveniently available to the supervisor, accurate and complete records of the drilling, redrilling, deepening, repairing, plugging, or abandoning of all wells and of all other well operations, and of all alterations to casing. These records shall show all the formations penetrated, the content and character of oil, gas, or water in each formation, and the kind, weight, size, and landed depth of casing used in drilling each well on the leased lands, and any other information obtained in the course of well operations.

(b) Within 15 days after the completion of any well and within 15 days after the completion of any further operations on it, the lessee shall transmit to the supervisor copies of these records on forms furnished by the supervisor. (For reports to be made by all lessees or their designated operators, see §§ 221.57 to 221.65.)

(c) The lessee shall take such samples and make such tests and surveys as may be required by the supervisor with a view to determining conditions in the well and obtaining information concerning materials (formations) drilled and shall furnish such characteristic samples of each formation or substance, or reports thereon, as may be requested by the supervisor. The lessee shall gage the production of oil, gas, and water from individual wells continuously or at reasonably frequent intervals to the satisfaction of the supervisor.

(d) The lessee shall also submit in duplicate such other reports and records of operations as may be required and in the manner and form prescribed by the supervisor.

(e) Upon request and in the manner and form prescribed by the supervisor the lessee shall furnish a copy of the daily drilling report, a plat showing the location, designation, and status of all wells on the leased lands, together with such other pertinent information as the supervisor may require.

§ 221.24 Precautions necessary in areas where high pressures are likely to exist.

When drilling in "wildcat" territory, or in any field where high pressures are likely to exist, the lessee shall take all necessary precautions for keeping the well under control at all times and shall provide at the time the well is started the proper high-pressure fittings and equipment; under such conditions the conductor string of casing must be cemented throughout its length, unless other procedure is authorized or prescribed by the supervisor, and all strings of casing must be securely anchored.

§ 221.25 Cable tool drilling precautions.

When drilling with cable tools, the lessee shall provide at lease one properly prepared slush pit, into which must be deposited mud and cuttings from clay or shale free of sand that will be suitable for the mudding of a well. When necessary or required, the lessee shall provide a

second pit for sand pumpings and other materials obtained from the well during the process of drilling that are not suitable for mudding.

§ 221.26 Rotary tool drilling precautions.

When drilling with rotary tools, the lessee shall provide, when required by the supervisor, an auxiliary mud pit or tank of suitable capacity and maintain therein a supply of mud having the proper characteristics for emergency use in case of blowouts or lost circulation.

§ 221.27 Vertical drilling.

The lessee shall drill substantially vertical wells, material deviation from the vertical being permitted only on written approval of the supervisor and where interests in other properties will not be unfairly affected.

§ 221.28 Water shut-offs; formation tests.

(a) By approved methods, the lessee shall shut off and exclude all water from any oil- or gas-bearing stratum to the satisfaction of the supervisor, and to determine the effectiveness of such operations, the lessee shall make a casing and a water shut-off test before suspending drilling operations or drilling into the oil or gas and completing the well.

(b) The lessee shall test for commercial productivity all formations that give evidence of carrying oil or gas, the test to be made to the satisfaction of and in a manner approved in advance by the supervisor. Unless otherwise specifically approved by the supervisor, formation tests shall be made at the time the formations are penetrated and in the absence of excessive back pressure from a column of water or mud fluid. Records of such tests shall be furnished in duplicate.

§ 221.29 Protection of upper productive strata.

The lessee shall not deepen an oil or gas well for the purpose of producing oil or gas from a lower stratum

until all upper productive strata are protected to the satisfaction of the supervisor.

§ 221.30 Open flows and control of "wild" wells.

The lessee shall take reasonable precautions to prevent any oil, gas, or water well from blowing open, or "wild", and shall take immediate steps and exercise due diligence to bring under control any such well or burning oil or gas well.

§ 221.31 Emulsion and dehydration.

The lessee shall complete and maintain his wells in such mechanical condition and operate them in such manner as to prevent, as far as possible, the formation of emulsion, or so-called B. S., and the infiltration of water. If the formation of emulsion, or B. S., or the infiltration of water, cannot be prevented or if all or any part of the product is unmarketable by reason thereof or on account of any impurity or foreign substance, the lessee shall put into marketable condition, if commercially feasible, all products produced from the leased land and pay royalty thereon without recourse to the lessor for deductions on account of costs of treatment or of costs of shipping. To avoid excessive losses from evaporation, oil shall not be heated to temperatures above the minimum required to put the oil into marketable condition. If excessive temperatures are required to break down an emulsion, then other means of dehydration must be utilized. Under such circumstances the supervisor must be consulted, and his approval obtained.

§ 221.32 Pollution and surface damage.

The lessee shall not pollute streams or damage the surface or pollute the underground water of the leased or other land. If useless liquid products of wells cannot be treated or destroyed or if the volume of such products is too great for disposal by usual methods without damage, the supervisor must be consulted, and the useless liquids disposed of by some method approved by him.

§ 221.33 Gaging and storing oil.

All production run from leased lands shall be gaged or measured according to methods approved by the supervisor. The lessee shall provide tanks located on the leasehold, unless otherwise approved by the supervisor, suitable for containing and measuring accurately all crude oil produced from the wells and shall furnish to the supervisor at least two acceptable positive copies of 100 percent-capacity tank tables. Meters for measuring oil must be first approved by the supervisor, and tests of their accuracy shall be made when directed by that official. The lessee shall not, except during an emergency and except by special permission of the supervisor, confirmed in writing, permit oil to be stored or retained in earthen reservoirs or in any other receptacle in which there may be undue waste of oil.

§ 221.34 Well abandonment.

(a) The lessee shall promptly plug and abandon or condition as a water well any well on the leased land that is not used or useful for the purposes of the lease, but no productive well shall be abandoned until its lack of capacity for further profitable production of oil or gas has been demonstrated to the satisfaction of the supervisor. Before abandoning a well the lessee shall submit to the supervisor a statement of reasons for abandonment and his detailed plans for carrying on the necessary work, together with duplicate copies of the log, if it has not already been submitted. A well may be abandoned only after receipt of written approval by the supervisor, in which the manner and method of abandonment shall be approved or prescribed. Equipment shall be removed and premises at the well-site shall be properly conditioned immediately after plugging operations are completed on any well.

(b) In case the lessee of lands of the United States strikes water while drilling, instead of oil or gas, and

the water is of sufficient quantity and suitable quality to be valuable and usable at a reasonable cost, the Secretary may take over the well as provided in section 40 of the Mineral Leasing Act approved June 16, 1934, 48 Stat. 977, 30 U.S.C. 299a. If a satisfactory agreement is reached, the lessee may condition the well for a water well in lieu of plugging and abandonment.

(c) Drilling equipment shall not be removed from any suspended drilling well without first securing the written consent of the supervisor.

§ 221.35 Waste Prevention; beneficial use.

The lessee is obligated to prevent the waste of oil or gas and to avoid physical waste of gas the lesser shall consume it beneficially or market it or return it to the productive formation. If waste or gas occurs the lessee shall pay the lessor the full value of all gas wasted by blowing, release, escape, or otherwise at a price not less than 5 cents for each 1,000 cubic feet, unless, on application by the lessee, such waste of gas under the particular circumstances involved shall be determined by the Secretary to be sanctioned by the laws of the United States and of the State in which it occurs. The production of oil and gas shall be restricted to such amount as can be put to beneficial use with adequate realization of values, and in order to avoid excessive production of either oil or gas, when required by the Secretary, shall be limited by the market demand for gas or by the market demand for oil.

§ 221.36 Accidents and fires.

The lessee shall take all reasonable precautions to prevent accidents and fires, shall notify the supervisor within 24 hours of all accidents or fires on the leased land, and shall submit a full report thereon within 15 days.

§ 221.37 Workmanlike operations.

The lessee shall carry on all operations and maintain the property at all times in a safe and workmanlike man-

ner, having due regard for the preservation and the conservation of the property and for the health and safety of employees. The lessee shall take reasonable steps to prevent and shall remove accumulations of oil or other materials deemed to be fire hazards from the vicinity of well locations and lease tanks, and shall remove from the property or store in orderly manner all scrap or other materials not in use.

§ 221.38 Sales contracts; division orders.

The lessee shall file with the supervisor triplicate (quadruplicate for production of restricted Indian lands or naval petroleum reserves) executed copies of all contracts for the disposition of all products of the leased land except that portion used for purposes of production on the leased land or unavoidably lost, and he shall not sell or otherwise dispose of said products except in accordance with a sales contract, division order, or other arrangement first approved, as provided in § 221.13.

§ 221.39 Relief from operating, royalty, and rental requirements.

Applications for any modification authorized by law of the operating requirements of a lease for lands of the United States shall be filed in triplicate (quintuplicate for applications involving leases for lands within the naval petroleum reserves) with the supervisor, and shall include a full statement of the circumstances that render such modification necessary or proper. Applications for any modification authorized by law of the royalty or rental requirements of a lease for lands of the United States shall be filed in triplicate in the office of the supervisor.

CROSS REFERENCE: For regulations of the Bureau of Land Management relating to royalty and rental relief, and suspension of operations and production, see 43 CFR Parts 3100 to 3104.

[13 FR 9496, Dec. 31, 1948]

§ 221.40 Royalty and rental payments.

(a) When due in money, the lessee shall tender all payments of rental and royalty by check or draft on a solvent bank, or by money order drawn to the order of the appropriate receiving officer, in accordance with statements rendered by the supervisor pursuant to § 221.12, or in the case of public-land leases in accordance with instructions of the Bureau of Land Management.

(b) If the lessor elects to take royalty in oil or gas, unless otherwise agreed upon, such royalty shall be delivered on the leasehold, by the lessee to the order of and without cost to the lessor, as instructed by the supervisor. Upon the lessor's request, storage for royalty oil for 30 days after the end of the calendar month in which the royalty accrues, shall be furnished free of charge. Storage shall be provided on the leased lands or at a place mutually agreed upon by the supervisor and the lessee.

§ 221.41 Surface rights on Indian lands.

Lessees of Indian land shall have only such surface rights as are specifically granted in the lease, but additional rights may be exercised under written agreement with the owner, such agreement to be subject to the prior approval of the superintendent of the Indian agency having jurisdiction. On demand of the supervisor, pipe lines on Indian land shall be buried below plow depth.

§ 221.42 Costs or damages.

The lessee shall pay all costs or damages assessed under the provisions of the regulations in this part.

CROSS REFERENCE: For other liabilities of the lessee in case of default, see also §§ 221.53 to 221.58.

MEASUREMENT OF PRODUCTION AND COMPUTATION OF ROYALTIES

§ 221.43 Measurement of oil.

The volume of production shall be computed in terms of barrels of clean oil of 42 standard United States gal-

lons of 231 cubic inches each, on the basis of meter measurements (meter must be approved by supervisor), or tank measurements of oil-level differences, made and recorded to the nearest quarter inch of 100-percent-capacity tables, or with such greater accuracy as shall be required by the supervisor, and subject to the following corrections.

(a) *Correction for impurities.* The percentage of impurities (water, sand, and other foreign substances not constituting a natural component part of the oil) shall be determined to the satisfaction of the supervisor, and the observed gross volume of oil shall be corrected to exclude the entire volume of such impurities.

(b) *Temperature correction.* The observed volume of oil corrected for impurities shall be further corrected to the standard volume at 60° F. in accordance with Table 2 of Circular C-410 of the National Bureau of Standards (March 4, 1936), or any revisions thereof and any supplements thereto, or any close approximation thereof approved by the supervisor.

(c) *Gravity determination.* The gravity of the oil at 60° F. shall be determined in accordance with Table 1 of Circular C-410 of the National Bureau of Standards (March 4, 1936), or any revisions thereof and any supplements thereto.

(d) *Lease production, pipe-line runs.* For the convenience of the lessor and lessee, monthly statements of production and royalty shall be based in general on production recorded in pipeline runs or other shipments. When shipments are infrequent or do not approximate actual production, the supervisor may require statements of production and royalty to be made on such other basis as he may prescribe, gains or losses in volume of storage being taken into account when appropriate. Evidence of all shipments of oil shall be furnished by pipe-line or other run tickets signed by representatives of the lessee and of

the purchaser who have witnessed the measurements reported and the determinations of gravity, temperature, and the percentage of impurities contained in the oil. Signed run tickets shall be filed with the supervisor within 5 days after the oil has been run.

§ 221.44 Measurement of gas.

Gas of all kinds (except gas used for purposes of production on the leasehold or unavoidably lost) is subject to royalty, and all gas shall be measured by meter (preferably of the orificemeter type) unless otherwise agreed to by the supervisor. All gas meters must be approved by the supervisor and installed at the expense of the lessee at such places as may be agreed to by the supervisor. For computing the volume of all gas produced, sold, or subject to royalty, the standard of pressure shall be 10 ounces above an atmospheric pressure of 14.4 pounds to the square inch, regardless of the atmospheric pressure at the point of measurement, and the standard of temperature shall be 60° F. All measurements of gas shall be adjusted by computation to these standards, regardless of the pressure and temperature at which the gas was actually measured, unless otherwise authorized in writing by the supervisor.

§ 221.45 Determination of gasoline content of natural gas.

Tests to determine the gasoline content of gas delivered to plants manufacturing gasoline are required to check plant efficiency and to obtain an equitable basis for allocating the gasoline output of any plant to the several sources from which the gas treated is derived. The gasoline content of the gas delivered to each gasoline plant treating gas from leased lands shall be determined periodically by field tests, as required by the supervisor, to be made at the place and by the methods approved by him and under his supervision.

§ 221.46 Quantity basis for computing royalties on natural gasoline, butane, propane, and other liquid hydrocarbon substances extracted from gas.

The primary quantity basis for computing monthly royalties on casinghead or natural gasoline, butane, propane, or other liquid hydrocarbon substances extracted from gas is the monthly net output of the plant at which the substances are manufactured, "net output" being defined as the quantity of each such substance that the plant produces for sale.

(a) If the net output of a plant is derived from the gas obtained from only one leasehold, the quantity of gasoline or other liquid hydrocarbon substances of which computations of royalty for the lease are based is the net output of the plant.

(b) If the net gasoline output of a plant is derived from gas obtained from several leaseholds producing gas of uniform gasoline content, the proportion of net output of gasoline allocable to each lease as a basis for computing royalty will be determined by dividing the amount of gas delivered to the plant from each leasehold by the total amount of gas delivered to the plant from all leaseholds.

(c) If the net gasoline output of a plant is derived from gas obtained from several leaseholds producing gas of diverse gasoline content, the proportion of net output of gasoline allocable to each leasehold as a bais for computing royalty will be determined by multiplying the amount of gas delivered to the plant from the leaseholds by the gasoline content of the gas and dividing the arithmetical product thus obtained by the sum of the similar arithmetical products separately obtained for all leaseholds from which gas is delivered to the plant.

(d) If the net output of butane, propane, or other liquid hydrocarbon substances of a plant is derived from gas obtained from several leaseholds, the proportion of net output of such substances allocable to each leasehold as

a basis for computing royalty will be determined by substituting the butane, propane, or other liquid hydrocarbon content for the gasoline content and following the method outlined in paragraph (b) or (c) of this section, which ever is applicable: *Provided,* That when in the judgment of the supervisor it is impracticable to test gas to determine the content of butane, propane, or other liquid hydrocarbon substances, the gasoline content will be used in determining the proportion of the net output of such substances allocable to each leasehold.

(e) The supervisor is authorized, whenever in his judgment neither method prescribed in paragraph (b) and (c) of this section is practicable, to estimate the production of natural gasoline, butane, propane, or other liquid hydrocarbon substances from any leasehold from: (1) The quantity of gas produced from the leasehold and transmitted to the extraction plant, (2) the gasoline, butane, propane, or other liquid hydrocarbon content of such gas as determined by test, and (3) a factor based on plant efficiency or recovery and so determined as to insure full protection of the royalty interest of the lessor.

§ 221.47 Value basis for computing royalties.

The value of production, for the purpose of computing royalty shall be the estimated reasonable value of the product as determined by the supervisor, due consideration being given to the highest price paid for a part or for a majority of production of like quality in the same field, to the price received by the lessee, to posted prices and to other relevant matters. Under no circumstances shall the value of production of any of said substances for the purposes of computing royalty be deemed to be less than the gross proceeds accruing to the lessee from the sale thereof or less than the value computed on such reasonable unit value as shall have been determined by the Secretary. In the absence of good reason to the contrary, value computed on the basis of the highest price per barrel, thousand cubic feet, or gallon paid or offered

at the time of production in a fair and open market for the major portion of like-quality oil, gas, or other products produced and sold from the field or area where the leased lands are situated will be considered to be a reasonable value.

§ 221.48 Royalty rates on oil; flat-rate leases.

The royalty on crude oil shall be the percentage (established by the terms of the lease) of the value or amount of the crude oil produced from the leased lands.

§ 221.49 Royalty rates on oil; sliding- and step-scale leases (public land only).

Sliding- and step-scale royalties are based on the average daily production per well. The supervisor shall specify which wells on a leasehold are commercially productive, including in that category all wells, whether produced or not for which the annual value of permissible production would be greater than the estimated reasonable annual lifting cost, but only wells which yield a commercial volume of production during at least part of the month shall be considered in ascertaining the average daily production per well. The average daily production per well for a lease is computed on the basis of a 28-, 29-, 30-, or 31-day month (as the case may be), the number of wells on the leasehold counted as producing and the gross production from the leasehold. (Tables for computing royalty on the sliding-scale and on the step-scale basis may be obtained upon application to the supervisor.) The supervisor will determine which commercially productive wells shall be considered each month as producing wells for the purpose of computing royalty in accordance with the following rules, and in his discretion may count as producing any commercially productive well shut-in for conservation purposes:

(a) For a previously producing leasehold, count as producing for every day of the month each previously producing well that produced 15 days or more during the

month, and disregard wells that produced less than 15 days during the month.

(b) Wells approved by the supervisor as input wells shall be counted as producing wells for the entire month if so used 15 days or more during the month and shall be disregarded if so used less than 15 days during the month.

(c) When the initial production of a leasehold is made during the calendar month, compute royalty on the basis of producing well-days.

(d) When a new well is completed for production on a previously producing leasehold and produces for 10 days or more during the calendar month in which it is brought in, count such new wells as producing every day of the month, in arriving at the number of producing well-days. Do not count any new well that produces for less than 10 days during the calendar month.

(e) Consider "head wells" that make their best production by intermittent pumping or flowing as producing every day of the month, provided they are regularly operated in this manner, with approval of the supervisor.

(f) For previously producing leaseholds on which no wells produced for 15 days or more, compute royalty on a basis of actual producing well-days.

(g) For previously producing leaseholds on which no wells were producing during the calendar month but from which oil was shipped, compute royalty at the same royalty percentage as that of the last preceding calendar month in which production and shipments were normal.

(h) Rules for special cases not subject to definition, such as those arising from averaging the production from two distinct sands or horizons when the production of one sand or horizon is relatively insignificant compared to that of the other, shall be made by the supervisor as need arises.

(i) (1) In the following summary of operations on a typical leasehold for the month of June, the wells considered for the purpose of computing royalty on the entire production of the property for the months are indicated.

Well No.	Record	Count (marked x)
1	Produced full time for 30 days	x
2	Produced for 26 days; down 4 days for repairs	x
3	Produced for 28 days; down June 5, 12 hours, rods, June 14, 6 hours, engine down, June 25, 24 hours June 26, 24 hours, pulling rods and tubing	x
4	Produced for 12 days; down June 13 to 30	
5	Produced for 8 hours every other day (head well)	x
6	Idle producer (not operated)	
7	New well, completed June 17, produced for 14 days	x
8	New well, completed June 22 produced for 9 days	

(2) In this example there are eight wells on the leasehold, but wells 4, 6, and 8 are not counted in computing royalties. Wells 1, 2, 3, 5, and 7 are counted as producing for 30 days. The average production per well per day is determined by dividing the total production of the leasehold for the month (including the oil produced by wells 4 and 8) by 5, the number of wells counted as producing, and dividing the quotient thus obtained by the number of days in the month.

§ 221.50 Royalty on gas.

The royalty on gas shall be the percentage established by the terms of the lease of the value or amount of the gas produced.

(a) Royalty accrues on dry gas, whether produced as such or as residue gas after the extraction of gasoline.

(b) If the lessee derives revenue on gas from two or more products, royalty normally will be collected on all such products.

(c) For the purpose of computing royalty the value of wet gas shall be either the gross proceeds accruing to the lessee from the sale thereof or the aggregate value determined by the Secretary of all commodities, including residue gas, obtained therefrom, whichever is greater.

§ 221.51 Royalty on casing-head or natural gasoline, butane, propane, or other liquid hydrocarbon substances extracted from gas.

A royalty as provided in the lease shall be paid on the value of one-third (or the lessee's portion if greater than one-third) of all casing-head or natural gasoline, butane, propane, or other liquid hydrocarbon substances extracted from the gas produced from the leasehold. The value of the remainder is an allowance for the cost of manufacture, and no royalty thereon is required. The value shall be so determined that the minimum royalty accruing to the lessor shall be the percentage established by the lease of the amount or value of all extracted hydrocarbon substances accruing to the lessee under an arrangement, by contract or otherwise, for extraction and sale that has been approved by the supervisor:

(a) When a minimum price established by the Secreary is used in determining the value of natural gasoline accruing to the lessee, the volume of such gasoline may be corrected when deemed necessary by the supervisor to such standard and by such method as may be approved by the supervisor, in order that volumetric differences between natural gasolines of various specifications may be equitably adjusted.

(b) The present policy is to allow the use of a reasonable amount of dry gas for operation of the gasoline plant, the amount allowed being determined or approved by the supervisor, but no allowance shall be made for boosting residue gas, or other expenses incidental to marketing.

§ 221.52 Royalty on drip gasoline or other natural condensate.

The royalty on all drip gasoline, or other natural condensate recovered from gas produced from the leased lands without resort to manufacturing process shall be the same percentage as provided in the lease for other oil, except that such substance, if processed in a casinghead gasoline plant shall be treated for royalty purposes as though it were gasoline.

PROCEDURE IN CASE OF DEFAULT BY LESSEE

§ 221.53 Shutting down operations; lease cancellations.

The supervisor has authority to shut down any operation and place under seal any property or equipment for failure to comply with the oil and gas operating regulations in this part or orders issued under this part, to enter upon any leasehold and perform any operation that the lessee fails to perform when ordered so to do in writing, and to recommend cancellation of the lease and forfeiture under the bond for noncompliance with the applicable law, lease terms, and regulations.

§ 221.54 Liquidated damages.

Administrative costs arising out of certain defaults or violations of orders requiring the performance of certain duties by lessees, as set forth in the regulations in this part constitute loss or damage to the United States the amount of which is difficult or impracticable of ascertainment. Therefore, the following amounts shall be deemed to cover such loss or damage and shall be payable upon receipt of notice from the oil and gas supervisor of such loss or damage: *Provided,* That as to paragraph (f) of this section the specified loss or damage shall be applicable to each week or fraction thereof during which the violation continues and as to paragraph (h) of this section the specified loss or damage shall be applicable to each

day or fraction thereof during which the violation continues:

(a) For failure to perform any operation ordered in writing by the supervisor, if said operation is thereafter performed by or through the supervisor, the actual cost of performance thereof and an additional 25 percent to compensate the Government for administrative costs.

(b) For failure to maintain inviolate any seal placed upon any property or equipment by the supervisor, $50 for each such violation.

(c) For failure to file notice of intention and to obtain approval before starting to drill, or for failure to file notice and obtain approval before making any changes in the originally approved notice of intention, $25 for each violation.

(d) For failure to file notice and to obtain approval before repairing, redrilling, deepening, plugging-back, plugging, or abandoning any well, in pulling or altering casing, stimulating production by vacuum, acid, or shot, or gas, air, or water injection, or using any well or formation for gas storage or water disposal, $25 for each violation.

(e) For failure to mark wells or derricks, $10 for each violation.

(f) For failure to install required high-pressure fittings and equipment, to cement conductor string, or to anchor properly all strings of casing, $50 for each violation.

(g) For failure to construct and maintain in proper condition slush or mud pits, $10 for each violation.

(h) For failure to comply with § 221.32, $25 for each violation.

(i) For failure to file sales contracts or division orders as required by lease terms, $25 for each violation, and

for failure to submit pipe-line run tickets, or other proper evidence of disposal as required by these regulations, $10 for each violation.

(j) For failure to file the following reports within the time specified in the regulations in this part, or within such other time designated in writing by the supervisor, $10 for each violation:

(1) Log of well, subsequent report of drilling, redrilling, deepening, plugging-back, plugging and abandonment, making water shut-off or formation test, stimulating production by acid or shot.

(2) Lessee's Monthly Report of Operations. Daily Report of Gas-Producing Wells, when required. Lessee's Statement of Oil and Gas Runs and Royalties.

(3) Special forms or reports as required by the supervisor.

§ 221.55 Payment of damages.

(a) Payment or request for payment for any of the damages assessed for administrative costs under the regulations in this part shall not relieve the lessee from compliance with the provisions of the regulations in this part, or for liability for waste or any other damage. A waiver of any particular cause for the payment of damages shall not be construed as precluding the assessment of damages for any other cause herein specified or for the same cause occurring at any other time.

(b) Damages shall be paid in the manner and as directed by the supervisor.

§ 221.56 Damages to Indian property.

Damages to lands, crops, buildings, and other improvements on Indian land shall be assessed by the superintendant and payments for such damages shall be made to the superintendent.

Reports To Be Made by All Lessees (Including Operators)

§ 221.57 General requirements.

Information required to be submitted in accordance with the regulations in this part shall be furnished in the manner and form prescribed in the regulations in this part or as directed by the supervisor. Prescribed standard forms in general use are described in §§ 221.58-221.64. Copies of such forms can be obtained from the supervisor and must be filled out completely and filed punctually with that official. Failure of the lessee to submit the information and reports required herein constitutes noncompliance with the terms of the regulations in this part and is cause for the assessment of specific damages as prescribed by the regulations in this part and the cancellation of the lease.

§ 221.58 Sundry notices and reports on wells (Form 9-331A Public; Form 9-331B Indian).

Forms 9-331A and 9-331B cover all notices of intention and all subsequent reports pertaining to individual wells except those for which special blanks are provided. The forms may be used for any of the purposes listed thereon, or a special heading may be inserted in the blank to adapt it for use for similar purposes. Any written notice of intention to do work or to change plans previously approved must be filed in triplicate, unless otherwise directed, and must reach the supervisor and receive his approval before the work is begun. The lessee is responsible for receipt of the notice by the supervisor in ample time for proper consideration and action. If, in case of emergency, and notice is given orally or by wire, and approval is obtained, the transaction shall be confirmed in writing as a matter of record. The following paragraphs illustrate some of the uses to which Forms 9-331A and 9-331B may be put and indicate the requirements with respect to each use.

(a) *Notice of intention to drill.* The notice of intention to drill a well must be filed with the supervisor and approval received before the work is begun. This notice must give the location, in feet, and direction from the nearest lines of established public survey; the altitude of the ground and derrick floor above sea level and how obtained; and the geologic name of the surface formation. Under the heading "Details of Work", the proposed drilling and casing plan should be outlined in detail. Essential information includes type of tools, proposed depth to which the well will be drilled, estimated depths to the top of important markers, estimated depths at which water, oil, gas, and mineral beds are expected, the proposed casing record, including the size and weight of casing, the depth at which each string is to be set, and the amount of cement and mud to be used. Information also shall be given relative to the drilling plan, such as making drill-stem tests, drilling in with oil, using reversed circulation, perforating opposite pays, using special types of mud in rotary drilling, coring at specified depths, and using electric logging together with any other information which may be required by the supervisor.

(b) *Notice of intention to change plans.* Where unexpected conditions necessitate any change in the plans of proposed work already approved, complete details of the changes must be submitted to the supervisor and approval thereof obtained before the work is undertaken.

(c) *Notice of date for casing and water shut-off test.* The protection and segregation of oil, gas, or water-bearing formations is an important item of conservation, and the supervisor will witness all casing and water shut-off tests. Notice must be filed with the supervisor in advance of the date on which the lessee expects to make such test. Later by agreement the exact time shall be fixed. The casing test and the test of water shut-off must be approved before further drilling can proceed. In the event

of failure, casing must be repaired or replaced or recemented, whichever the conditions may require.

(d) *Subsequent report of casing and water shut-off test.* Within 15 days after making a casing or water shut-off test, the results of the test must be reported. The report must give complete and accurate details, amount of mud and cement used, lapse of time between running and cementing the casing and making the test, method of testing, and results.

(e) *Notice of intention to redrill, repair, or condition well.* Before repairing, deepening, or conditioning a well, a detailed written statement of the plan of work must be filed with the supervisor and approval obtained before the work is started. In work that affects only rods, pumps, or tubing, or other routine work, such as cleaning out to previous total depth, no report is necessary unless specifically required by the supervisor.

(f) *Subsequent report of redrilling, repairing, or conditioning.* Within 15 days after completion of the repair work a detailed report of work done and the results obtained should be filed. Such report shall show the amount of production of oil, gas, and water, both before and after the work is done, and shall also include a complete statement of the work accomplished and methods employed, including all dates.

(g) *Notice of intention to use explosive or chemicals.* Before using explosive or chemicals (shooting or acidizing) in any well, whether for increasing production or in drilling, repair, or abandonment, notice of intention shall be filed and approval obtained before the work is done. When such notice of intention forms a part of a notice of intention to redrill, repair, or abandon a well, the supervisor may accept such notice in lieu of a separate notice of intention to use explosive or chemicals. The notice of intention to use explosive or chemicals must be accompanied by the complete log of the well to date, provided the

complete log has not previously been filed, and must state the object of the work to be done, the amount and nature of the material to be used, its exact location and distribution in the well by depths, the method of localizing its effects, and the name of the company that is to do the work. The notice shall also contain an accurate statement of the dates and daily production of oil, gas, and water from the well for each of the last preceding 10 producing days.

(h) *Subsequent report of use of explosive or chemicals.* After using explosive or chemicals in any well a subsequent report must be filed with the supervisor. This report shall be filed separately within 15 days after the work is done, unless such report is included in the log as a part of a report of other subsequent work done or as a part of an abandonment report any one of which shall have been filed within that period. The subsequent report of use of explosive or chemicals shall include a statement of the amount and the nature of the material used, its exact location and distribution in the well by depths, and the method used to localize its effects. The report shall also contain an accurate statement of the dates and daily production of oil, gas, and water for each of the last 10 producing days preceding the use of explosive or chemicals and a similar statement of production after the work is done. In addition, this report must include other pertinent information, such as the depth to which the well was cleaned out, the time spent in bailing and cleaning out, and any injuries to the casing or well.

(i) *Notice of intention to pull, perforate, or otherwise alter casing.* If any casing is to be pulled, perforated, or otherwise altered, notice of intention must be filed and approved before the work is started. Such notice must give full details of the contemplated work, stating fully what results are anticipated. A notice of intention to perforate the casing shall state the conditions of the well that make such work desirable; whether it is to be ripped

or shot, the depth, number, and size of shots, or if ripped, the depths of the rips proposed; the production of oil, gas, and water; and, if a log of the well has not already been filed, the notice should be accompanied by a duplicate copy of the log showing all casing seats as well as all water strata and all oil and gas shows.

(j) *Subsequent report of pulling, perforating, or otherwise altering casing.* If any casing has been pulled, perforated, or otherwise altered, the results of the work should be reported within 15 days after the completion of such work, stating exactly what was done and the results obtained, including any change in production. The report of perforating casing also should include the number, depth, and size of shots, the date shot, and who did the shooting. If ripped, the depths and number of rips should be stated. The production of oil, gas, and water obtained by the work should be shown.

(k) *Notice of intention to abandon well.* Before beginning abandonment work on any well, whether drilling well, oil or gas well, water well, or so-called dry hole, notice of intention to abandon shall be filed with the supervisor and approval obtained before the work is started. The notice must show the reason for abandonment and must be accompanied by a complete log, in duplicate, of the well to date, provided the complete log has not been filed previously, and must give a detailed statement of the proposed work, including such information as kind, location, and length of plugs (by depths), and plans for mudding, cementing, shooting, testing, and removing casing, as well as any other pertinent information.

(l) *Subsequent report of abandonment.* After a well is abandoned or plugged a subsequent record of work done must be filed with the supervisor. This report shall be filed separately within 15 days after the work is done. The report shall give a detailed account of the manner in

which the abandonment or plugging work was carried out, including the nature and quantities of materials used in plugging and the location and extent (by depths) of the plugs of different materials; records of any tests or measurements made and of the amount, size, and location (by depths) of casing left in the well; and a detailed statement of the volume of mud fluid used, and the pressure attained in mudding. If an attempt was made to part any casing, a complete report of the methods used and results obtained must be included.

§ 221.59 Log and history of well (Form 9-330).

The lessee shall furnish in duplicate, on Form 9-330, to the supervisor, not later than 15 days after the completion of each well, a complete and accurate log and history, in chronological order, of all operations conducted on the well. If a log is compiled for geologic information from cores or formation samples, duplicate copies of such log shall be filed in addition to the regular log. Duplicate copies of all electric logs, temperature surveys, or direction surveys shall be furnished. The lessee shall require the drillers, whether using company labor or contract labor, to record accurately the depth, character, fluid content, and fluid levels, where possible, of each formation as it is penetrated, together with all other pertinent information obtained in drilling the well. The practice of compiling well logs from memory, after the work has been completed, will not be permitted.

§ 221.60 Monthly report of operations Form 9-329 Public; Form 9-329A Indian).

A separate report of operations for each lease must be made on Form 9-329 for public land and on Form 9-329A for Indian land, for each calendar month, beginning with the month in which drilling operations are initiated, and must be filed in duplicate with the supervisor on or before the 6th day of the succeeding month, unless an extension of time for the filing of such report is granted by the

supervisor. The report on this form shall disclose accurately all operations conducted on each well during each month, the status of operations on the last day of the month, and a general summary of the status of operations on the leased lands, and the report must be submitted each month until the lease is terminated or until omission of the report is authorized by the supervisor. It is particularly necessary that the report shall show for each calendar month:

(a) The lease be identified by inserting the name of the United States land office and the serial number, or in the case of Indian land the lease number and lessor's name, in the space provided in the upper right corner;

(b) Each well be listed separately by number, its location be given by 40-acre subdivision (¼ ¼ sec. or lot), section number, township, range, and meridian;

(c) The number of days each well produced, whether oil or gas, and the number of days each input well was in operation be stated;

(d) The quantity of oil, gas, and water produced, the total amount of gasoline, and other lease products recovered and other required information. When oil and gas, or oil, gas, and gasoline, or other hydrocarbons are concurrently produced from the same use, separate reports on this form should be submitted for oil and for gas and gasoline, unless otherwise authorized or directed by the supervisor.

(e) The depth of each active or suspended well, and the name, character, and depth of each formation drilled during the month, the date each such depth was reached, the date and reason for every shut-down, the names and depths of important formation changes and contents of formations, the amount and size of any casing run since last report, the dates and results of any tests such as production, water shut-off, or gasoline content, and any other noteworthy information on operations not specifically provided for in the form.

(f) The footnote must be completely filled out as required by the supervisor. If no runs or sales were made during the calendar month, the report must so state.

§ 221.61 Daily report of gas-producing wells (Form 9-352).

Unless otherwise directed by the supervisor, the readings of all meters showing production of natural gas from leased lands shall be submitted daily on Form 9-352, together with the meter charts. After a check has been had the meter charts will be returned.

§ 221.62 Statement of oil and gas runs and royalties (Form 9-361 Public; Form 9-361A Indian).

When directed by the supervisor, a monthly report shall be made by the lessee in duplicate, on Form 9-361 or 9-361A, showing each run of oil, and sales of gas, gasoline, other lease products, and the royalty accruing therefrom to the lessor. When use of this form is required it must be completely filled out and sworn to.

§ 221.63 Royalty and rental remittance (Form 9-614A Indian).

Form 9-614A, completely filled out and signed, shall be submitted to the supervisor in triplicate and shall accompany each remittance covering payments of royalty or rental on Indian lands.

§ 221.64 Royalty and rental remittance (Form 11ND Naval Petroleum Reserves).

Form 11ND, completely filled out and signed, must accompany each remittance covering payments of royalty or rental on Naval Petroleum Reserves. The remittance and the original form shall be sent direct to the Property Accounting Officer, United States Navy, Bureau of Supplies and Accounts, Navy Deuartment, Washington, D.C. 20360, and the duplicate and triplicate copies of the form shall be sent to the oil and gas supervisor.

§ 221.65 Special forms or reports.

When special forms or reports other than those referred to in the regulations in this part may be necessary, instructions for the filing of such forms or reports will be given by the supervisor.

§ 221.66 Appeals.

Orders or decisions issued under the regulations in this part may be appealed from as provided in Part 290 of this chapter. Compliance with any such order or decision shall not be suspended by reason of an appeal having been taken unless such suspension is authorized in writing by the Director or the Board of Land Appeals (depending upon the official before whom the appeal is pending) and then only upon a determination that such suspension will not be detrimental to the lessor or upon submission and acceptance of a bond deemed adequate to indemnify the lessor from loss or damage.

[38 FR 10001, Apr. 23, 1973]

§ 221.67 Effective date; repeal of prior regulations.

The regulations in this part shall become effective on the 1st day of June 1942, and shall supersede the oil and gas operating regulations of November 1, 1936, as amended, 30 CFR, 1938 ed., 221.1 to 221.56, except as to leases and unit agreements in force and effect on June 1, 1942, to which the regulations in this part are not applicable.[1]

§ 221.80 Late payment or underpayment charges.

The failure to make timely or proper payment of any monies due pursuant to leases, permits, and contracts sub-

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[1] Not applicable on said effective date to lands acquired under the Act known as the Appalachian Forest Act of March 1, 1911, 36 Stat. 961, to lands in national parks, to lands withdrawn or reserved for military or naval uses or purposes, except naval petroleum reserves, or to lands within the Osage Indian Reservation.

ject to these regulations will result in the collection of the amount due and, with the exception of underpayments for advance royalty on future gas production made timely and otherwise in accordance with the instructions provided the payee, in the assessment and collection of a late payment charge. The late payment charges assessed will be computed on the basis of the amount past due for each 30-day period or portion thereof that the payment or underpayment is late. In the absence of a specific lease, permit, or contract provision prescribing a different rate, the percentage assessment rate to be applied in these instances will be the rate calculated by the Department of the Treasury as the current value of funds to the Treasury based on a recent 3-month period. This rate will be prescribed in the Treasury Fiscal Requirements Manual Bulletins which are published prior to the first day of each calendar quarter for application to overdue or underpayments which occur during the succeeding calendar quarter.

Underpayments and payments which are received after the due date will be applied to the appropriate current charges for rentals; production and minimum royalties; assessments for liquidated damages; administrative fees and payments by purchasers of royalty taken-in-kind, or, to such other payments, fees, or assessments which a lessee/operator, permittee, or purchaser or royalty taken-in-kind is required to submit by a specified date.

The failure to remit past due amounts, including late payment charges, will result in the initiation of other enforcement proceedings.

[45 FR 84764, Dec. 23, 1980]

Redesignation Table Showing Relationship of Former 30 CFR Part 221 (1981) to Current 30 CFR Parts 202 to 206 (1985)

Secretarial Order No. 3087 dated December 3, 1982, as amended, declared that all functions related to royalty and mineral revenue management are the responsibility of the Minerals Management Service (MMS) and that all onshore minerals management functions on Federal and Indian lands are transferred to the Bureau of Land Management (BLM).

For the convenience of the user, the following table identifies regulations that MMS will retain and administer and sets forth new subchapter, part and subpart headings that reorganize and consolidate MMS regulations in a logical manner (48 FR 35639, Aug. 5, 1983).

Former 30 CFR section designations	New 30 CFR chapter II designations
	Subchapter A—Royalty Management
	Part 201—General
	Subpart A—General Provisions—[Reserved]
	Subpart B—Oil and Gas, General—[Reserved]
	Subpart C—Oil and Gas, Onshore
221.13	201.100 Responsibilities of the Associate Director for Royalty Management.
	Subpart D—Oil, Gas and Sulfur, Offshore—[Reserved]
	Subpart E—Coal—[Reserved]
	Subpart F—Other Solid Minerals—[Reserved]
	Subpart G—Geothermal Resources—[Reserved]
	Subpart H—Indian Lands [Reserved]
	Part 202—Royalty Rates and Rentals
	Subpart A—General Provisions—[Reserved]
	Subpart B—Oil and Gas, General—[Reserved]
	Subpart C—Oil and Gas, Onshore
221.100	202.100 Production records; rentals, royalties, and payments; drainage and waste.
221.106	202.101 Measurement of oil.
221.107	202.102 Measurement of gas.
221.111	202.103 Royalty rate on oil; flat-rate leases.
	Subpart D—Oil, Gas and Sulfur, Offshore
250.65	202.150 Royalty on oil.
256.55	202.151 Minimum royalty.
256.53	202.152 Royalties.
	Subpart E—Coal—[Reserved]

Former 30 CFR section designations	New 30 CFR chapter II designations
	Subpart F—Other Solid Minerals—[Reserved]
	Subpart G—Geothermal Resources—[Reserved]
	Subpart H—Indian Lands—[Reserved]
	Part 203—Relief or Reduction in Royalty Rates
	Subpart A—General Provisions—[Reserved]
	Subpart B—Oil and Gas, General—[Reserved]
	Subpart C—Oil and Gas, Onshore
221.104	203.100 Relief from operating, royalty, and rental requirements.
	Subpart D—Oil, Gas and Sulfur, Offshore
250.21	203.150 Reduction of royalty or net profit share.
	Subpart E—Coal
	203.200 Royalties.
	Subpart F—Other Solid Minerals—[Reserved]
	Subpart G—Geothermal Resources—[Reserved]
	Subpart H—Indian Lands—[Reserved]
	Part 206—Product Valuation
	Subpart A—General Provisions—[Reserved]
	Subpart B—Oil and Gas, General—[Reserved]
	Subpart C—Oil and Gas, Onshore
221.102	206.100 Waste prevention, beneficial use.
221.108	206.101 Determination of gasoline content of natural gas.
221.109	206.102 Quality basis for computing royalties on natural gasoline, butane, propane, and other liquid hydrocarbon substances extracted from gas.
221.110	206.103 Value basis for computing royalties.
221.112	206.104 Royalty rates on oil; sliding- and step-scale leases (Public land only).
221.113	206.105 Royalty on gas.
221.114	206.106 Royalty on casing-head or natural gasoline, butane, propane, or other liquid hydrocarbon substances extracted from gas.
221.115	206.107 Royalty on drip gasoline or other natural condensate.
	Subpart D—Oil, Gas and Sulfur, Offshore
250.64	206.150 Value basis for computing royalties.
250.66	206.151 Royalty on unprocessed gas.
250.67	206.152 Royalty on processed gas and constituent products.
	Subpart E—Coal [Reserved]
	Subpart F—Other Solid Minerals—[Reserved]
	Subpart G—Geothermal Resources
270.62	206.300 Value of geothermal production for computing royalties.
270.63	206.301 Computations of royalties.
	Subpart H—Indian Lands—[Reserved]

Redesignation Table Showing Relationship of Former 30 CFR Part 221 (1981) to Current 43 CFR Parts 3160-3165 (1985)

At 48 FR 36583, Aug. 12, 1983, 30 CFR Part 221 was redesignated as 43 CFR Part 3160. For the convenience of the user, the following table shows the relationship of the old CFR section numbers to the new CFR section numbers.

Old 30 CFR Part 221	New 43 CFR Part 3160
	Insert new part title—Part 3160—Onshore Oil and Gas Operations.
	Insert new Subpart 3160—Onshore Oil and Gas Operations—General.
221.1 (First sentence)	3160.0-1 Purpose.
221.1 (Second sentence)	3160.0-4 Objectives.
221.1 (Third sentence)	3160.0-2 Policy.
	Insert new § 3160.0-3 Authority.
221.2	3160.0-5.
221.2-1	Inserted as a note immediately after Part title.
221.3	3160.0-7.
221.4-221.9	Remove.
	Insert new subpart 3161—Jurisdiction and Responsibility.
221.10	3161.1.
221.11	3161.2.
221.12	Remove.
221.13	Remove.
221.14	3164.1.
221.15	3164.2.
221.16-221.19	Remove.
	Insert Subpart 3162—Requirements for Lessees and Operators.
221.20	3162.1.
221.21	3162.3.
221.22	3162.2.
221.23	3162.3-1.
221.24	3162.6.
221.25	3162.5-2.
221.26	3162.4-2.
221.27	3162.3-2.
221.28	3162.3-3.
221.29	3162.3-4.

Old 30 CFR Part 221	New 43 CFR Part 3160
	Insert new § 3162.5—Environment and safety.
221.30	3162.5-1.
221.31	3162.5-3.
	Insert new § 3162.4—Records and reports.
221.32	3162.4-1.
221.33	3162.8.
	Insert new § 3162.7—Measurement, disposition and protection of production.
221.34	3162.7-2.
221.35	3162.7-3.
221.36	3162.7-1.
221.37	3162.7-4.
221.38-221.49	Remove.
	Insert new Subpart 3163—Non-Compliance and Assessments.
221.50	3163.1.
221.51	3163.2.
221.52	3163.3.
221.53	3163.4.
221.54	3163.5.
221.55-221.59	Remove.
	Insert new Subpart 3164—Special Provisions.
221.60	3164.3.
221.61	3164.4.
221.62-221.69	Remove.
	Insert new Subpart 3165—Relief, Conflicts and Appeals.
221.70	3165.1.
221.71	3165.2.
221.72	3165.3.
221.73	3165.4.
221.74-221.99	Remove.
221.104	3165.1-1.
221.117	3162.4-3.

Part 206—Product Valuation

AUTHORITY: The Act of February 25, 1920 (30 U.S.C. 181, et seq.) as amended; the Act of May 21, 1930 (30 U.S.C. 301-306); the Mineral Leasing Act for Acquired Lands (30 U.S.C. 351-359), as amended; the Act of March 3, 1909 (25 U.S.C. 396), as amended; the Act of May 11, 1938 (25 U.S.C. 396a-396q), as amended; the Act of February 28, 1891 (25 U.S.C. 397), as amended; the Act of May 29, 1924 (25 U.S.C. 398); the Act of March 3, 1927 (25 U.S..C 398a-398e); the Act of June 30, 1919 (25 U.S.C. 399), as amended; R.S. § 441 (43 U.S.C. 1457), see also Attorney General's Opinion of April 2, 1941 (40 Op. Atty. Gen. 41); the Federal Property and Administrative Services Act of 1949 (40 U.S.C. 471 et seq.), as amended; the National Environmental Act of 1969 (42 U.S.C. 4321 et seq.); as amended; the Act of December 12, 1980 (Pub. L. 96-514, 94 Stat. 2964); and the Hydrocarbon Leasing Act of 1981 (Pub. L. 97-78, 95 Stat. 1070); the Outer Continental Shelf Lands Act (43 U.S.C. 1331, et seq.) as amended; the Geothermal Act of 1970 (30 U.S.C. 1001 et seq.), as amended; section 2 of Reorganization Plan No. 3 of 1950 (64 Stat. 1262); Secretarial Order No. 3071 of January 19, 1982, as amended; and Secretarial Order No. 3087, as amended.

SOURCE: 47 FR 47773-47775, Oct. 27, 1982, unless otherwise noted. Redesignated at 48 FR 35641, Aug. 5, 1983.

§ 206.100 Waste prevention; beneficial use.

The lessee is obligated to prevent the waste of oil or gas, and to avoid physical waste of gas, the lessee shall consume it beneficially or market it or return it to the productive formation. If waste of gas occurs, the lessee

shall pay the lessor the full value of all gas wasted by blowing, release, escape, or otherwise at a price not less than 5 cents for each 1,000 cubic feet unless, on application by the lessee, such waste of gas under the particular circumstances involved shall be determined by the Secretary to be sanctioned by the laws of the laws of the United States and of the State in which it occurs.

§ 206.101 Determination of gasoline content of natural gas

Tests to determine the gasoline content of gas delivered to plants manufacturing gasoline are required to check plant efficiency and to obtain an equitable basis for allocating the gasoline output of any plant to the several sources from which the gas treated in derived.

§ 206.102 Quantity basis for computing royalties on natural gasoline, butane, propane, and other liquid hydrocarbon substances extracted from gas.

The primary quantity basis for computing monthly royalties on casinghead or natural gasoline, butane, propane, or other liquid hydrocarbon substances extracted from gas is the monthly net output of the plant at which the substances are manufactured, "net output" being defined as the quantity of each substance that the plant produces for sale.

(a) If the net output of a plant is derived from the gas obtained from only one leasehold, the quantity of gasoline or other liquid hydrocarbon substances of which computations of royalty for the lease are based is the net output of the plant.

(b) If the net gasoline output of a plant is derived from gas obtained from several leaseholds producing gas of uniform gasoline content, the proportion of net output of gasoline allocable to each lease as a basis for computing royalty will be determined by dividing the amount

of gas delivered to the plant from each leasehold by the total amount of gas delivered by the plant from all leaseholds.

(c) If the net gasoline output of a plant is derived from gas obtained from several leaseholds producing gas of diverse gasoline content, the proportion of net output of gasoline allocable to each leasehold as a basis for computing royalty will be determined by multiplying the amount of gas delivered to the plant from the leaseholds by the gasoline content of the gas and dividing the arithmetical product thus obtained by the sum of the simular arithmetical products separately obtained for all leaseholds from which gas is delivered to the plant.

(d) If the net output of butane, propane, or other liquid hydrocarbon substances of a plant is derived from gas obtained from several leaseholds, the proportion of net output of such substances allocable to each leasehold as a basis for computing royalty will be determined by substituting the butane, propane, or other liquid hydrocarbon content for the gasoline content and following the method outlined in paragraph (b) or (c) of this section, whichever is applicable: *Provided*, That when in the judgment of the Associate Director, it is impracticable to test gas to determine the content of butane, propane, or other liquid hydrocarbon substances, the gasoline content will be used in determining the proportion of the net output of such substances allocable to each leasehold.

(e) The Associate Director is authorized, whenever in his judgment neither method prescribed in paragraph (b) and (c) of this section is practicable, to estimate the production of natural gasoline, butane, propane, or other liquid hydrocarbon substances from any leasehold from (1) the quantity of gas produced from the leasehold and transmitted to the extraction plant, (2) the gasoline, butane, propane, or other liquid hydrocarbon content of

such gas as determined by test, and (3) a factor based on plant efficiency or recovery and so determined as to insure full protection of the royalty interest of the lessor.

§ 206.103 Value basis for computing royalties.

The value of production, for the purpose of computing royalty, shall be the estimated reasonable value of the product as determined by the Associate Director due consideration being given to the highest price paid for a part or for a majority of production of like quality in the same field, to the price received by the lessee, to posted prices, and to other relevant matters. Under no circumstances shall the value of production of any of said substances for the purposes of computing royalty be deemed to be less than the gross proceeds accruing to the lessee from the sale thereof or less than the value computed on such reasonable unit value as shall have been determined by the Secretary. In the absence of good reason to the contrary, value computed on the basis of the highest price per barrel, thousand cubic feet, or gallon paid or offered at the time of production in a fair and open market for the major portion of like-quality oil, gas, or other products produced and sold from the field or area where the leased lands are situated will be considered to be a reasonable value.

§ 206.104 Royalty rates on oil; sliding- and step-scale leases (public land only).

Sliding- and step-scale royalties are based on the average daily production per well. The Supervisor shall specify which wells on a leasehold are commercially productive, including in that category all wells, whether produced or not, for which the annual value of permissible production would be greater than the estimated reasonable annual lifting cost, but only wells which yield a commercial volume of production during at least part of

the month shall be considered in ascertaining the average daily production per well. The average daily production per well for a lease is computed on the basis of a 28-, 29-, 30-, or 31-day month (as the case may be), the number of wells on the leasehold counted as producing, and the gross production from the leasehold. (Tables for computing royalty on the sliding-scale and on the step-scale basis may be obtained upon application to the Associate Director.) The Supervisor will determine which commercially productive wells shall be considered each month as producing wells for the purpose of computing royalty in accordance with the following rules, and in his discretion may count as producing any commercially productive well shut-in for conservation purposes.

(a) For a previously producing leasehold, count as producing for every day of the month each previously producing well that produced 15 days or more during the month, and disregard wells that produced less than 15 days during the month.

(b) Wells approved by the Supervisor as input wells shall be counted as producing wells for the entire month if so used 15 days or more during the month and shall be disregarded if so used less than 15 days during the month.

(c) When the initial production of a leasehold is made during the calendar month, compute royalty on the basis of producing well-days.

(d) When a new well is completed for production on a previously producing leasehold and produces for 10 days or more during the calendar month in which it is brought in, count such new wells as producing every day of the month, in arriving at the number of producing well-days. Do not count any new well that produces for less than 10 days during the calendar month.

(e) Consider "head wells" that make their best production by intermittent pumping or flowing as producing every day of the month, provided they are regularly operated in this manner, with approval of the Supervisor.

(f) For previously producing lease-holds on which no wells produced for 15 days or more, compute royalty on a basis of actual producing well-days.

(g) For previously producing leaseholds on which no wells were producing during the calendar month but from which oil was shipped, compute royalty at the same royalty percentage as that of the last preceding calendar month in which production and shipments were normal.

(h) Rules for special cases not subject to definition, such as those arising from averaging the production from two distinct sands or horizons when the production of one sand or horizon is relatively insignificant compared to that of the other, shall be made by the Associate Director as need arises.

(i) (1) In the following summary of operations on a typical leasehold for the month of June, the wells considered for the purpose of computing royalty on the entire production of the property for the months are indicated.

(2) In this example, there are eight wells on the leasehold, but wells Nos. 4, 6, and 8 are not counted in computing royalties. Wells Nos. 1, 2, 3, 5, and 7 are counted as producing for 30 days. The average production per well per day is determined by dividing the total production of the leasehold for the month (including the oil produced by wells 4 and 8) by 5, the number of wells counted as producing, and dividing the quotient thus obtained by the number of days in the month.

Well No.	Record	Count (marked X)
1.....	Produced full time for 30 days.	X.
2.....	Produced for 26 days; down 4 days for repairs.	X.
3.....	Produced for 28 days; down June 5, 12 hours, rods; June 14, 6 hours, engine down; June 26, 24 hours, pulling rods and tubing.	X.
4.....	Produced for 12 days; down June 13 to 30.	
5.....	Produced for 8 hours every day (head well).	X.
6.....	Idle producer (not operated).	
7.....	New well, completed June 17; produced for 14 days.	X.
8.....	New well, completed June 22; produced for 9 days.	

§ 206.105 Royalty on gas.

The royalty on gas shall be the percentage established by the terms of the lease of the value or amount of the gas produced.

(a) Royalty accrues on dry gas, whether produced as such or as residue gas after the extraction of gasoline.

(b) If the lessee derives revenue on gas from two or more products, a royalty normally will be collected on all such products.

(c) For the purpose of computing royalty, the value of wet gas shall be either the gross proceeds accruing to the lessee from the sale thereof or the aggregate value determined by the Secretary of all commodities, including residue gas, obtained therefrom, whichever is greater.

§ 206.106 Royalty on casing-head or natural gasoline, butane, propane, or other liquid hydrocarbon substances extracted from gas.

A royalty as provided in the lease shall be paid on the value of one-third (or the lessee's portion if greater than one-third) of all casing-head or natural gasoline, butane, propane, or other liquid hydrocarbon substances extracted from the gas produced from the leasehold. The value of the remainder is an allowance for the cost of manufacture, and no royalty thereon is required. The value shall be so determined that the minimum royalty accruing to the lessor shall be the percentage established by the lease of the amount or value of all extracted hydrocarbon substances accruing to the lessee under an arrangement, by contract or otherwise, for extraction and sale that has been approved by the Associate Director.

(a) When a minimum price established by the Secretary is used in determining the value of natural gasoline accruing to the lessee, the volume of such gasoline may be corrected when deemed necessary by the Associate Director to such standard and by such method as may be approved by the Associate Director, in order that volumetric differences between natural gasolines of various specifications may be equitably adjusted.

(b) The present policy is to allow the use of a reasonable amount of dry gas for operation of the gasoline plant, the amount allowed being determined or approved by the Associate Director, but no allowance shall be made for boosting residue gas, or other expenses incidental to marketing.

§ 206.107 Royalty on drip gasoline or other natural condensate.

The royalty on all drip gasoline, or other natural condensate recovered from gas produced from the leased lands without resort to manufacturing process, shall be the same percentage as provided in the lease for other oil, except that such substance, if processed in a casing-head gasoline plant, shall be treated for royalty purposes as though it were gasoline.

Bureau of Land Management, Interior

Part 3160—Onshore Oil and Gas Operations

Subpart 3160—Onshore Oil and Gas Operations—General

AUTHORITY: The Act of February 25, 1920 (30 U.S.C. 181, et seq.), as amended; the Act of May 21, 1930 (30 U.S.C. 301-306); the Mineral Leasing Act for Acquired Lands (30 U.S.C. 351-359), as amended; the Act of March 3, 1909 (25 U.S.C. 396), as amended; the Act of May 11, 1938 (25 U.S.C. 396a-396q), as amended; the Act of February 28, 1891 (25 U.S.C. 397), as amended; the Act of May 29, 1924 (25 U.S.C. 398); the Act of March 3, 1927 (25 U.S.C. 398a-398e); the Act of June 30, 1919 (25 U.S.C. 399), as amended; R.S. § 441 (43 U.S.C. 1457), see also Attorney General's Opinion of April 2, 1941 (40 Op. Atty. Gen. 41); the Federal Property and Administrative Services Act of 1949 (40 U.S.C. 471, et seq.), as amended; the National Environmental Policy Act of 1969 (42 U.S.C. 4321, et seq.), as amended; the Act of December 12, 1980 (Pub. L. 96-514, 94 Stat. 2964); and the Combined Hydrocarbon Leasing Act of 1981 (Pub. L. 97-78, 95 Stat. 1070; the Federal Oil and Gas Royalty Management Act of 1982 (30 U.S.C. 1701); and the Indian Mineral Development Act of 1982 (25 U.S.C. 2102)).

SOURCE: 47 FR 47765, Oct. 27, 1982, unless otherwise noted. Redesignated at 48 FR 36583-36586, Aug. 12, 1983.

EDITORIAL NOTE 1: See Redesignation Table No. 1 appearing the Finding Aids section of this volume.

EDITORIAL NOTE 2: Nomenclature changes to this part appear at 48 FR 36584-36586, Aug. 12, 1983.

§ 3160.0-1 Purpose.

The regulations in this part govern operations associated with the exploration, development and production of oil and gas deposits from leases issued or approved by the United States, restricted Indian land leases and those under the jurisdiction of the Secretary of the Interior by law or administrative arrangement, including the National Petroleum Reserve—Alaska.

[48 FR 36583, Aug. 12, 1983]

§ 3160.0-2 Policy.

The regulations in this part are administered under the direction of the Director of the Bureau of Land Management; except that as to lands within naval petroleum reserves, they shall be administered under such official as the Secretary of Energy shall designate.

[48 FR 36584, Aug. 12, 1983]

§ 3160.0-3 Authority.

The Mineral Leasing Act, as amended and supplemented (30 U.S.C. 181 et seq.), the Act of May 21, 1930 (30 U.S.C. 301-306), the Mineral Leasing Act for Acquired Lands, as amended (30 U.S.C. 351-359), the Act of March 3, 1909, as amended (25 U.S.C. 396), the Act of May 11, 1938, as amended (25 U.S.C. 396-396q), the Act of February 28, 1891, as amended (25 U.S.C. 397), the Act of May 29, 1924 (25 U.S.C. 398), the Act of March 3, 1927 (25 U.S.C. 398a-398e), the Act of June 30, 1919, as amended (25 U.S.C. 399), R.S. § 441 (43 U.S.C. 1457), the Attorney General's Opinion of April 2, 1941 (40 Op Atty. Gen. 41), the Federal Property and Administrative Services Act of 1949, as amended (40 U.S.C. 471 et seq.), the National Environmental Policy Act of 1969, as amended (42 U.S.C. 4321 et seq.), the Act of December 12, 1980 (94 Stat. 2964), the Combined

Hydrocarbon Leasing Act of 1981 (95 Stat. 1070), the Federal Oil and Gas Royalty Management Act of 1982 (30 U.S.C. 1701), the Indian Mineral Development Act of 1982 (25 U.S.C. 2102), and Order Number 3087, dated December 3, 1982, as amended on February 7, 1983 (48 FR 8983) under which the Secretary consolidated and transferred the onshore minerals management functions of the Department, except mineral revenue functions and the responsibility for leasing of restricted Indian lands, to the Bureau of Land Management.

[48 FR 36583, Aug. 12, 1983]

§ 3160.0-4 Objectives.

The objective of these regulations is to promote the orderly and efficient exploration, development and production of oil and gas.

[48 FR 36583, Aug. 12, 1983]

§ 3160.0-5 Definitions.

Authorized Representative. Any entity or individual authorized by the Secretary to perform duties by cooperative agreement, delegation, or contract.

Avoidably lost. Avoidably lost production shall mean the venting or flaring of produced gas without the prior authorization, approval, ratification, or acceptance of the Supervisor and the loss of produced oil or gas when the Supervisor determines that such loss occurred as a result of (1) negligence on the part of the lessee, or (2) the failure of the lessee to take all reasonable measures to prevent and/or control the loss, or (3) the failure of the lessee to comply fully with the applicable lease terms and regulations, applicable orders and notices, or the written orders of the Supervisor, or (4) any combination of the foregoing.

Director. The Director of the Bureau of Land Management.

Federal Lands. All lands and interests in lands owned by the United States which are subject to the mineral leasing laws, including mineral resources or mineral estates reserved to the United States in the conveyance of a surface or nonmineral estate.

Fresh water. Water containing not more than 1,000 ppm of total dissolved solids, provided that such water does not contain objectionable levels of any constituent that is toxic to animal, plant, or aquatic life, unless otherwise specified in applicable notices or orders.

Lease. Any contract, profit-share arrangement, joint venture, or other agreement issued or approved by the United States under a mineral leasing law that authorizes exploration for, extraction of, or removal of oil or gas.

Lease Site. Any lands, including the surface of a severed mineral estate, on which exploration for, or extraction and removal of, oil or gas is authorized pursuant to a lease.

Lessee. The party authorized by or through a lease or an approved assignment thereof, to explore for, develop and produce oil and gas on the lease site in accordance with the lease terms, regulations, and law. For convenience of reference throughout this part, the term lessee also refers to and includes the owners of approved operating rights and designated operators.

Lessor. The party to a lease who holds legal or beneficial title to the mineral estate in the leased lands.

Maximum ultimate economic recovery. The recovery of oil and gas from the leased lands which a prudent operator could be expected to make from that field or reservoir given existing knowledge of reservoir and other pertinent facts and utilizing common industry practices for primary, secondary, and tertiary recovery operations.

Notice to lessees and operators (NTL). A written notice issued by the DMM. NTL's implement the regulations in this part and operating orders, and serve as isntructions on specific item(s) of importance within a Region or portion thereof.

Onshore oil and gas order. A formal numbered order issued by the Director that implements the regulations in this part.

Operator. The party that has control or management of operations on the leased land or a portion thereof. The operator may be a lessee, holder of rights under an approved operating agreement, or designated operator.

Paying well. A paying well is a well that is capable of producing oil or gas of sufficient value to exceed direct operating costs and the costs of lease rentals or minimal royalty.

Person. Any individual, firm, corporation, association, partnership, consortium or joint venture.

Production in paying quantities. Lease production of oil and/or gas of sufficient value to exceed direct operation costs and the cost of lease rentals or minimum royalty.

Superintendent. The Superintendent of an Indian Agency, or other officer authorized to act in matters of record and law with respect to oil and gas leases on restricted Indian lands.

Waste of oil or gas. Any act or failure to act by the lessee that is not sanctioned by the Supervisor as necessary for proper development and production and which results in (1) a reduction in the quantity or quality of oil and gas ultimately producible from a reservoir under prudent and proper operations, or (2) avoidable surface loss of oil or gas.

[47 FR 47765, Oct. 27, 1982. Redesignated and amended at 48 FR 36583, 36584, Aug. 12, 1983; 49 FR 37363, Sept. 21, 1984]

§ 3160.0-7 Cross references.

25 CFR Parts 221, 212, 213, and 227
30 CFR Group 200
40 CFR Chapter V
43 CFR Parts 2, 4, and 1820 and Groups 3000, 3100 and 3500

[48 FR 36584, Aug. 12, 1983]

Subpart 3161—Jurisdiction and Responsibility

§ 3161.1 Jurisdiction.

Subject to the supervisory authority of the Secretary and the Director, all operations conducted on or for the benefit of a Federal or Indian oil and gas lease by, or on behalf of, the lessee are subject to the regulations in this part and are under the direction of the authorized officer having jurisdiction of the leased lands.

[47 FR 47765, Oct. 27, 1982. Redesignated and amended at 48 FR 36583, 36584, Aug. 12, 1983]

§ 3161.2 Responsibility of the authorized officer.

The authorized officer is authorized and directed to approve unitization, communitization, gas storage and other contractual agreements for Federal lands; to assess compensatory royalty; to approve suspensions of operations or production, or both; to issue NTL's; to approve and monitor other operator proposals for drilling, development or production of oil and gas; to perform technical and procedural reviews; to assess monetary penalties or liquidated damages; to provide technical information and advice relative to oil and gas development and operations on Federal and Indian lands; to enter into cooperative agreements with States, Federal agencies and Indian tribes relative to oil and gas development and operations; to approve, inspect and regulate the operations that are subject to the regulations in this part; to require compliance with lease terms, with the regulations in this title

and all other applicable regulations promulgated under the cited laws; and to require that all operations be conducted in a manner which protects other natural resources and the environmental quality, protects life and property and results in the maximum ultimate recovery of oil and gas with minimum waste and with minimum adverse effect on the ultimate recovery of other mineral resources. The authorized officer may issue written or oral orders to govern specific lease operations. Any such oral orders shall be confirmed in writing by the authorized officer within 10 working days from issuance thereof. Before approving operations on leasehold, the authorized officer shall determine that the lease is in effect, that the operator is authorized to conduct such operations, that acceptable bond coverage has been provided and that the proposed plan of operations is sound both from a technical and environmental standpoint.

[48 FR 36584, Aug. 12, 1983]

§ 3161.3 Inspections.

(a) The authorized officer shall establish procedures to ensure that each Federal and Indian lease site which is producing or is expected to produce significant quantities of oil or gas in any year or which has a history of noncompliance with applicable provisions of law or regulations, lease terms, orders or directives shall be inspected at least once annually. Similarly, each lease site on non-Federal or non-Indian lands subject to a formal agreement such as a unit or communitization agreement which has been approved by the Department of the Interior and in which the United States or the Indian lessors share in production shall be inspected annually whenever any of the foregoing criteria are applicable.

(b) In accomplishing the inspections, the authorized officer may utilize Bureau Personnel, may enter cooperative agreements with States of Indian Tribes, may delegate the inspection authority to any State, or may contract with non-Federal Governmental entities. Any co-

operative agreement, delegation or contractual arrangement shall not be effective without concurrence of the Secretary and shall include applicable provisions of the Federal Oil and Gas Royalty Management Act.

[49 FR 37363, Sept. 21, 1984]

Subpart 3162—Requirements for Lessees and Operators

§ 3162.1 General requirements.

(a) The lessee shall comply with applicable laws and regulations; with the lease terms, Onshore Oil and Gas Orders, NTL's; and with other orders and instructions of the authorized officer. These include, but are not limited to, conducting all operations in a manner which ensures the proper handling, measurement, disposition, and site security of leasehold production; which protects other natural resources and environmental quality; which protects life and property; and which results in maximum ultimate economic recovery of oil and gas with minimum waste and with minimum adverse effect on ultimate recovery of other mineral resources.

(b) The lessee shall permit properly identified authorized representatives to enter upon, travel across and inspect lease sites and records normally kept on the lease pertinent thereto without advance notice. Inspections normally will be conducted during those hours when responsible persons are expected to be present at the operation being inspected. Such permission shall include access to secured facilities on such lease sites for the purpose of making any inspection or investigation for determining whether there is compliance with the mineral leasing laws, the regulations in this part, and any applicable orders, notices or directives.

(c) For the purpose of making any inspection or investigation, the Secretary or his authorized representative shall have the same right to enter upon or travel

across any lease site as the lessee or operator has acquired by purchase, condemnation or otherwise.

[47 FR 47765, Oct. 27, 1982. Redesignated and amended at 48 FR 36583, 36584, Aug. 12, 1983; 49 FR 37364, Sept. 21, 1984]

§ 3162.2 Drilling and producing obligations.

(a) The lessee shall drill diligently and produce continuously from such wells as are necessary to protect the lessor from loss of royalty by reason of drainage. The authorized officer may assess compensatory royalty under which the lessee will pay a sum determined as adequate to compensate the lessor for lessee's failure to drill and produce wells required to protect the lessor from loss through drainage by wells on adjacent lands. Any such assessment will be made after a review of available information relating to development of the leased lands. Such assessment is subject to termination or modification based upon the authorized officer's continuing review of such information.

(b) The lessee, at its election, may drill and produce other wells in conformity with any system of well spacing or production allotments affecting the field or area in which the leased lands are situated, and which is authorized and sanctioned by applicable law or by the authorized officer.

(c) After notice in writing, the lessee shall promptly drill and produce such other wells as the authorized officer may reasonably require in order that the lease may be properly and timely developed and produced in accordance with good economic operating practices.

§ 3162.3 Conduct of operations.

(a) Leasehold operations shall be conducted by the lessee or its designees. The lessee may authorize the actual conduct of operations in its behalf by designating another

party as operator in a manner and form acceptable to the authorized officer. Acceptance of an executed designation as authority for the designee to act for the lessee in matters relating to the conduct of lease operations does not relieve the lessee from the ultimate responsibility for compliance with applicable laws, regulations, lease terms, Onshore Oil and Gas Orders, NTL's, and the orders and instructions of the authorized officer. Lessees shall notify the authorized officer in writing when a designation of operator has been canceled. A designated operator cannot designate a different party as operator.

(b) The contractor or other person in charge of or conducting operations on a leasehold will be considered the agent of the lessee for such operations with full responsibility for acting on behalf of the lessee insofar as complying with applicable laws, regulations, the lease terms, NTL's, Onshore Oil and Gas Orders, and other orders and instructions of the authorized officer. The serving of orders, instructions, or notices on the contractor or other person in charge of conducting such operations on a leasehold, when delivered personally or by ordinary mail, will be deemed to be service upon the lessee. When served in this manner, a copy will be mailed to the lessee and the designated operator at their address of record.

§ 3162.3-1 Drilling applications and plans.

(a) Each well shall be drilled in conformity with an acceptable well-spacing program at a surveyed well location approved or prescribed by the authorized officer after appropriate environmental and technical reviews (see § 3162.5-1 of this title). An acceptable well-spacing program may be either (1) one which conforms with a spacing order or field rule issued by a State Commission or Board and accepted by the authorized officer, or (2) one which is located on a lease committed to a communitized or unitized tract at a location approved by the authorized officer, or (3) any other program established by the authorized officer.

(b) Any well drilled on restricted Indian land shall be subject to the location restrictions specified in the lease and/or Title 25 of the Code of Federal Regulations.

(c) The lessee shall submit to the authorized officer for approval an Application for Permit to Drill for each well. No drilling operations, nor surface disturbance preliminary thereto, may be commenced prior to the authorized officer's approval of the permit.

(d) The Application for Permit to Drill process shall be initiated at least 30 days before commencement of operations is anticipated. Prior to approval, the application must be administratively and technically complete. A complete application consists of Form 9-331C and the following attachments: (1) A drilling plan, which may already be on file, containing information required by paragraph (e) of this section and appropriate orders and notices, (2) evidence of bond coverage as required by Department of the Interior regulations, (3) designation of operator, where necessary, and (4) such other information as may be required by applicable orders and notices. If the process is initiated less than 30 days prior to the desired date of commencement of drilling operations, the process may not be completed by the desired date.

(e) Each drilling plan shall contain the information specified in applicable notices or orders, including a description of the drilling program, the surface and projected completion zone location, pertinent geologic data, expected problems and hazards and proposed mitigation, road and drillpad location and construction, methods for containment and disposal of waste material, plans for restoration of the surface, and other pertinent data as the authorized officer may require. A drilling plan may be submitted for a single well or for several wells which are proposed to be drilling to the same zone within a field or area of geologic and environmental similarity. A drilling plan may be modified from time to time as circum-

stances may warrant, with the approval of the authorized officer.

(f) Upon initiation of the Application for Permit to Drill process, the authorized officer will consult with the appropriate Federal Surface Management Agency and with other appropriate interested parties and will take one of the following actions within 30 days: (1) Approve the application as submitted or with appropriate modifications or stipulations; (2) return the application and advise the applicant of the reasons for disapproval; or (3) advise the applicant, either in writing or orally with subsequent written confirmation, of the reasons why final action will be delayed along with the date such final action can be expected.

§ 3162.3-2 Subsequent well operations.

(a) A plan proposing further well operations shall be submitted by the lessee on Form 9-331 for approval by the authorized officer prior to commencing operations to redrill, deepen, perform casing repairs, plug-back, alter casing, perform nonroutine fracturing jobs, recomplete in a different interval, perform water shut-off conversion to injection. A subsequent report on these operations also will be filed on Form 9-331. The authorized officer may prescribe that each plan contain all or a portion of the information set forth in § 3162.3-1 of this title.

(b) Unless additional surface disturbance is involved and if the operations conform to the standard of prudent operating practice, prior approval is not required for routine fracturing or acidizing jobs, or recompletion in the same interval; however, a subsequent report on these operations must be filed on Form 9-331.

(c) No prior approval or a subsequent report is required for well cleanout work, routine well maintenance, or bottom hole pressure surveys.

§ 3162.3-3 Other lease operations.

Prior to commencing any operation on the leasehold which will result in additional surface disturbance, other than those authorized under § 3162.3-1 or § 3162.3-2 of this title, the lessee shall submit a proposed plan of operations on Form 9-331 to the authorized officer for approval.

§ 3162.3-4 Well abandonment.

(a) The lessee shall promptly plug and abandon, in accordance with a plan first approved in writing or prescribed by the authorized officer, each newly completed or recompleted well in which oil or gas is not encountered in paying quantities or which, after being completed as a producing well, is demonstrated to the satisfaction of the authorized officer to be no longer capable of producing oil or gas in paying quantities, unless the authorized officer shall approve the use of the well as a service well for injection to recover additional oil or gas or for subsurface disposal of produced water. In the case of a newly drilled or recompleted well, the approval to abandon may be written or oral with written confirmation.

(b) Completion of a well as plugged and abandoned may also include conditioning the well as water supply source for lease operations or for use by the surface owner or appropriate Government Agency, when authorized by the authorized officer. All costs over and above the normal plugging and abandonment expense will be paid by the party accepting the water well.

(c) No well may be temporarily abandoned for more than 30 days without the prior approval of the authorized officer. The authorized officer may authorize a delay in the permanent abandonment of a well for a period of 12 months. When justified by the lessee, the authorized officer may authorize additional delays, no one of which may exceed an additional 12 months. Upon the removal of drilling or producing equipment from the site of a

well which is to be permanently abandoned, the surface of the lands disturbed in connection with the conduct of operations shall be rehabilitated or restored in accordance with a plan first approved or prescribed by the authorized officer.

§ 3162.4 Records and reports.

[48 FR 36583, Aug. 12, 1983]

§ 3162.4-1 Well records and reports.

(a) The lessee shall keep accurate and complete records with respect to all lease operations including, but not limited to, production facilities and equipment, drilling, producing, redrilling, deepening, repairing, plugging back, and abandonment operations, and other matters pertaining to operations. With respect to production facilities and equipment, the record shall include schematic diagrams as required by applicable orders and notices.

(b) Standard forms for providing basic data are listed in NOTE 1 at the beginning of this title. As noted on Form 9-330, two copies of all electric and other logs run on the well must be submitted to the authorized officer. Upon request, the lessee shall transmit to the authorized officer copies of such other records maintained in compliance with paragraph (a) of this section.

(c) Not later than the 5th business day after any well begins production on which royalty is due anywhere on a lease site or allocated to a lease site, or resumes production in the case of a will which has been off production for more than 90 days, the operator shall notify the authorized officer by letter or sundry notice, Form 3160-5, or orally to be followed by a letter or sundry notice, of the date on which such production has begun or resumed.

(d) All records and reports required by this section shall be maintained for 6 years from the date they were generated. In addition, if the Secretary, or his/her desig-

nee notifies the recordholder that the Department of the Interior has initiated or is participating in an audit or investigation involving such records, the records shall be maintained until the Secretary, or his/her designee, releases the recordholder from the obligation to maintain such records.

[47 FR 47765, Oct. 27, 1982. Redesignated and amended at 48 FR 36583, 36585, Aug. 12, 1983; 49 FR 37364, Sept. 21, 1984]

§ 3162.4-2 Samples, tests, and surveys.

(a) During the drilling and completion of a well, the lessee shall, when required by the authorized officer, conduct tests, run logs, and make other surveys reasonably necessary to determine the presence, quantity, and quality of oil, gas, other minerals, or the presence or quality of water; to determine the amount and/or direction of deviation of any well from the vertical; and to determine the relevant characteristics of the oil and gas reservoirs penetrated.

(b) After the well has been completed, the lessee shall conduct periodic well tests which will demonstrate the quantity and quality of oil and gas and water. The method and frequency of such well tests will be specified in appropriate notices and orders. When needed, the lessee shall conduct reasonable tests which will demonstrate the mechanical integrity of the downhole equipment.

(c) Results of samples, tests, and surveys approved or prescribed under this section shall be provided to the authorized officer without cost to the lessor.

§ 3162.4-3 Monthly report of operations (Form 9-329 Public; Form 329A Indian).

A separate report of operations for each lease shall be made on Form 9-329 for each calendar month, beginning

with the month in which drilling operations are initiated, and shall be filed in duplicate with the authorized officer on or before the 10th day of the second month following the production month, unless an extension of time for the filing of such report is granted by the authorized officer. The report on this form shall disclose accurately all operations conducted on each well during each month, the status of operations on the last day of the month, and a general summary of the status of operations on the leased lands, and the report shall be submitted each month until the lease is terminated or until omission of the report is authorized by the authorized officer. It is particularly necessary that the report shall show for each calendar month:

(a) The lease be identified by inserting the name of the United States land office and the serial number, or in the case of Indian land, the lease number and lessor's name, in the space provided in the upper right corner;

(b) Each well be listed separately by number, its location be given by 40-acre subdivision (¼ ¼ sec. or lot), section number, township, range, and meridian;

(c) The number of days each well produced, whether oil or gas, and the number of days each input well was in operation be stated;

(d) The quantity of oil, gas and water produced, the total amount of gasoline, and other lease products recovered, and other required information. When oil and gas, or oil, gas and gasoline, or other hydrocarbons are concurrently produced from the same lease, separate reports on this form should be submitted for oil and for gas and gasoline, unless otherwise authorized or directed by the authorized officer.

(e) The depth of each active or suspended well, and the name, character, and depth of each formation drilled during the month, the date each such depth was reached, the date and reason for every shut-down, the names and

depths of important formation changes and contents of formations, the amount and size of any casing run since last report, the dates and results of any tests such as production, water shut-off, or gasoline content, and any other noteworthy information on operations not specifically provided for in the form.

(f) The footnote shall be completely filled out as required by the authorized officer. If no runs or sales were made during the calendar month, the report shall so state.

[47 FR 47765, Oct. 27, 1982. Redesignated and amended at 48 FR 36583, 36586, Aug. 12, 1983]

§ 3162.5 Environment and safety.

[48 FR 36583, Aug. 12, 1983]

§ 3162.5-1 Environmental obligations.

(a) The lessee shall conduct operations in a manner which protects the mineral resources, other natural resources, and environmental quality. In that respect, the lessee shall comply with the pertinent orders of the authorized officer and other standards and procedures as set forth in the applicable laws, regulations, lease terms and conditions, and the approved drilling plan or subsequent operations plan. Before approving any Application for Permit to Drill submitted pursuant to § 3162.3-1 of this title, or other plan requiring environmental review, the authorized officer shall prepare an environmental record of review or an environmental assessment, as appropriate. These environmental documents will be used in determining whether or not an environmental impact statement is required and in determining any appropriate terms and conditions of approval of the submitted plan.

(b) The lessee shall exercise due care and diligence to assure that leasehold operations do not result in undue damage to surface or subsurface resources or surface im-

provements. All produced water must be disposed of by injection into the subsurface, by approved pits, or by other methods which have been approved by the authorized officer. Upon the conclusion of operations, the lessee shall restore or rehabilitate the disturbed surface in a manner approved or reasonably prescribed by the authorized officer.

(c) All spills or leakages of oil, gas, produced water, toxic liquids, or waste materials, blowouts, fires, personal injuries, and fatalities shall be reported by the lessee in accordance with these regulations and as prescribed in applicable order or notices. The lessee shall exercise due diligence in taking necessary measures, subject to approval by the authorized officer, to control and remove pollutants and to extinguish fires. A lessee's compliance with the requirements of the regulations in this part shall not relieve the lessee of the obligation to comply with other applicable laws and regulations.

(d) When reasonably required by the authorized officer, a contingency plan shall be submitted describing procedures to be implemented to protect life, property, and the environment.

(e) The lessee's liability for damages to third parties shall be governed by applicable law.

§ 3162.5-2 Control of wells.

(a) *Drilling wells.* The lessee shall take all necessary precautions to keep each well under control at all times, and shall utilize and maintain materials and equipment necessary to insure the safety of operating conditions and procedures.

(b) *Vertical drilling.* The lessee shall conduct drilling operations in a manner so that the completed well does not deviate significantly from the vertical without the prior written approval of the authorized officer. Significant deviation means a projected deviation of the well bore from the vertical of 10° or more, or a projected

bottom hole location which could be less than 200 feet from the spacing unit or lease boundary. Any well which deviates more than 10° from the vertical or could result in a bottom hole location less than 200 feet from the spacing unit or lease boundary without prior written approval must be promptly reported to the authorized officer. In these cases, a directional survey is required.

(c) *High pressure or loss of circulation.* The lessee shall take immediate steps and utilize necessary resources to maintain or restore control of any well in which the pressure equilibrium has become unbalanced.

(d) *Protection of fresh water and other minerals.* The lessee shall isolate freshwater-bearing and other usable water containing 5,000 ppm or less of dissolved solids and other mineral-bearing formations and protect them from contamination. Tests and surveys of the effectiveness of such measures shall be conducted by the lessee using procedures and practices approved or prescribed by the authorized officer.

§ 3162.5-3 Safety precautions.

The lessee shall perform operations and maintain equipment in a safe and workmanlike manner. The lessee shall take all precautions necessary to provide adequate protection for the health and safety of life and the protection of property. Compliance with health and safety requirements prescribed by the authorized officer shall not relieve the lessee of the responsibility for compliance with other pertinent health and safety requirements under applicable laws or regulations.

§ 3162.6 Well identification.

(a) Lessee shall properly identify in a conspicuous place each drilling, producing, or abandoned well, with the name of the operator, the lease serial number, the well number, the surveyed description of the well (either footages or the quarter-quarter section, the section, township,

and range), and, when specifically requested by the authorized officer, the name of the Indian allotted lessor preceding the lease serial number. The lessee shall maintain all well markings in a legible condition.

(b) All abandoned wells shall be marked with a permanent monument containing the information in (a). The well identification requirement for an abandoned well may be waived in writing by the authorized officer upon submission of a request by the surface owner or surface management agency.

§ 3162.7 Measurement, disposition, and protection of production.

[48 FR 36583, Aug. 12, 1983]

§ 3162.7-1 Disposition of production.

(a) The lessee shall put into marketable condition, if economically feasible, all oil, other hydrocarbons, gas, and sulphur produced from the leased land.

(b) Where oil accumulates in a pit, such oil must either be (1) recirculated through the regular treating system and returned to the stock tanks for sale, or (2) pumped into a stock tank without treatment and measured for sale in the same manner as from any sales tank in accordance with applicable orders and notices. In the absence of prior approval from the authorized officer, no oil should go to a pit except in an emergency. Each such occurrence must be reported to the authorized officer and the oil promptly recovered in accordance with applicable orders and notices.

(c) (1) Any person engaged in transporting by motor vehicle any oil from any lease site, or allocated to any such lease site, shall carry on his/her person, in his/her vehicle, or in his/her immediate control, documentation showing at a minimum; the amount, origin, and intended first purchaser of the oil.

(2) Any person engaged in transporting any oil or gas by pipeline from any lease site, or allocated to any lease site, shall maintain documentation showing, at a minimum, the amount, origin, and intended first purchaser of such oil or gas.

(3) On any lease site, any authorized representative who is properly identified may stop and inspect any motor vehicle that he/she has probable cause to believe is carrying oil from any such lease site, or allocated to such lease site, to determine whether the driver possesses proper documentation for the load of oil.

(4) Any authorized representative who is properly identified and who is accompanied by an appropriate law enforcement officer, or an appropriate law enforcement officer alone, may stop and inspect any motor vehicle which is not on a lease site if he/she has probable cause to believe the vehicle is carrying oil from a lease site, or allocated to a lease site, to determine whether the driver possesses proper documentation for the load of oil.

(d) The lessee shall conduct operations in such a manner as to prevent avoidable loss of oil and gas. A lessee shall be liable for royalty payments on oil or gas lost or wasted from a lease site, or allocated to a lease site, when such loss or waste is due to negligence on the part of the lessee of such lease, or due to the failure of the lessee to comply with any regulation, order or citation issued pursuant to this part.

(e) When requested by the authorized officer, the lessee shall furnish storage for royalty oil, on the leasehold or at a mutually agreed upon delivery point off the leased land without cost to the lessor, for 30 days following the end of the calendar month in which the royalty accrued.

(f) Any records generated under this section shall be maintained for 6 years from the date they were generated or, if notified by the Secretary, or his designee, that such records are involved in an audit or investigation, the records shall be maintained until the recordholder is

released by the Secretary from the obligation to maintain them.

[47 FR 47765, Oct 27, 1982. Redesignated and amended at 48 FR 36583, 36585, Aug. 12, 1983; 49 FR 37364, Sept. 21, 1984]

§ 3162.7-2 Measurement of oil.

All oil production shall be measured by tank gauging, positive displacement metering system, or other methods acceptable to the authorized officer, pursuant to methods and procedures prescribed in applicable orders and notices. Where production cannot be measured due to spillage or leakage, the amount of production shall be determined in accordance with the methods and procedures approved or prescribed by the authorized officer.

[47 FR 47765, Oct. 27, 1982. Redesignated and amended at 48 FR 36583, 36585, Aug. 12, 1983; 49 FR 37364, Sept. 21, 1984]

§ 3162.7-3 Measurement of gas.

All gas production shall be measured by orifice meters or other methods acceptable to the authorized officer on the lease pursuant to methods and procedures prescribed in applicable orders and notices. The measurement of the volume of all gas produced shall be adjusted by computation to the standard pressure and temperature of 14.73 psia and 60° F unless otherwise prescribed by the authorized officer, regardless of the pressure and temperature at which the gas is actually measured. Gas lost without measurement by meter shall be estimated in accordance with methods prescribed in applicable orders and notices.

[47 FR 47765, Oct. 27, 1982. Redesignated and amended at 48 FR 36583, 36585, Aug. 12, 1983; 49 FR 37364, Sept. 21, 1984]

§ 3162.7-4 Site security on Federal and Indian (except Osage) oil and gas leases.

(a) *Definitions—*

Appropriate valves. Those valves in a particular piping system, i.e., fill lines, equilizer lines, sales lines, circulating lines, drain lines, or other lines, that must be sealed during a given phase of operations.

Closed system. A piping arrangement from one or more source points to one or more other points in a system which does not have means of access, i.e., flat plugs, bullplugs, blanking caps, open-ended valves, or combinations thereof.

Effectively sealed. The placement of a seal in such a manner that the position of the sealed fitting may not be altered or the fitting removed from the system without the seal being destroyed.

Open system. A piping arrangement from one or more source points to one or more other points in a system which does have a means of access, i.e., flat plugs, bullplugs, blanking caps, open-ended valves, or combinations thereof.

Production phase. That period of time or mode of operation during which crude oil is delivered directly to or through production vessels to the storage facilities.

Sales phase. That period of time or mode of operation during which crude oil is removed from the storage facilities for sales, transportation or other purposes.

Seal. A device, uniquely numbered, which completely secures a fitting.

(b) *Minimum standards.* Each operator of a Federal or Indian (except Osage) lease shall comply with the following minimum standards:

(1) All appropriate valves on lines entering or leaving oil storage tanks shall be effectively sealed during the

production phase and during the sales phase. The piping and connections in a closed system which are tamper proof or tamper resistant are essentially protected from unauthorized or undocumented entry, but the piping and connections in an open system shall be protected. For a minimum of 6 years the operator shall maintain a record of seal numbers used and shall document on which valves or connections they were used as well as when they were installed and removed. The site facility diagram(s) shall show which valves will be sealed in which positions during both the production and sales phase, and shall show whether the piping is an open or closed system.

(2) Each Automatic Custody Transfer (ACT) system shall employ meters that have non-resettable totalizers. There shall be no by-pass piping around the ACT. Similarly, there shall be no by-pass piping around gas meters. Equipment which permits changing the orifice plate without bleeding the pressure off the gas meter run is not considered a by-pass.

(3) Where oil is sold via hand gauged volumes, the operator shall minimize the time that oil is stored on leases to that time needed to accumulate an economic run. The operator may retain that oil needed for use on the lease and to provide for delivery of royalty oil.

(4) The operator will deal promptly with any other accumulations of oil in pits or tanks in accordance with the provisions of § 3162.7-1 of this title and applicable NTL's or onshore orders.

(5) The operator, with reasonable frequency, shall regularly inspect all leases, units, and communitized areas to determine site security and production volumes. The operator shall retain records of such inspections and measurements for 6 years. Such records and measurements shall be available to any authorized officer or authorized representative upon request.

(6) All facilities at which oil is stored shall be clearly identified with a sign that contains the name of the op-

erator, the lease serial number (or communitization or unit agreement identification), and, in public land States, the quarter-quarter, section, township, and range. On Indian leases, the sign also shall include the name of the appropriate Tribe and whether the lease is tribal or allotted. In addition, each storage tank shall be clearly identified by a unique number. The identification shall be maintained in legible condition and shall be clearly apparent to any person at or approaching the sales or transportation point. With regard to the quarter-quarter designation and the unique tank number, any such designation established by state law or rule will satisfy this requirement. Any facility identification which is in existence on the effective date of this rule and which meets the basic information required herein will satisfy this paragraph until such sign is replaced.

(7) Any person removing oil from a facility by motor vehicle shall possess the identification documentation required by applicable NTL's or operating orders while the oil is being removed and transported.

(8) Theft or mishanding of oil from a Federal or Indian lease shall be reported to the authorized officer as soon as discovered but not later than the next business day. Said report shall include an estimate of the volume of oil involved. Operators also are expected to report such thefts promptly to local law enforcement agencies and internal company security.

(9) Any operator may request the authorized officer to approve a variance from any of the minimum standards prescribed by this section. The authorized officer shall approve a variance if the proposed alternative meets or exceeds the objective of the applicable standard.

(c) *Site security plans.* (1) Site security plans, which include the operator's plan for complying with the minimum standards enumerated in paragraph (b) of this section, shall be completed and the existing facilities shall be in compliance with the plan on September 9, 1983. For

facilities constructed after September 9, 1983 conformance with existing plans shall be established or new plans shall be completed no later than 30 days of completion of construction or first production, whichever occurs first, and on that date the facilities shall be in compliance with the plan. At the operator's option, a single plan may include all of the operator's leases, unit and communitized areas, within a single BLM district, provided the plan clearly identifies each lease, unit, or communitized area included within the scope of the plan and the extent to which the plan is applicable to each lease, unit, or communitized area so identified.

(2) The operator shall retain the plan but shall notify the authorized officer of its completion and which leases, unit and commuitized areas are involved. Such notification is due at the time the plan is completed as required by (c) (1) of this section. Such notification shall include the location and normal business hours of the office where the plan will be maintained.

(3) The plan shall include the frequency and method of the operator's inspection and production volume recordation. The authorized officer may, upon examination, require adjustment of the method or frequency of inspection.

(d) *Site facility diagrams.* (1) Facility diagrams shall be filed with the authorized officer no later than September 9, 1983 for those facilities in existence on that date. Thereafter, facility diagrams shall be filed within 30 days after new measurement facilities are installed or existing facilities are modified.

(2) No format is prescribed for facility diagrams. They should be prepared on 8½″ x 11″ paper, if possible, and be legible and comprehensible to a person with ordinary working knowledge of oilfield operations and equipment.

(3) A site facility diagram shall reflect the actual conditions at the site and shall clearly identify the vessels,

piping (indicating whether piping is a closed or open system), and metering system which apply to the handling and disposal of oil, gas, and water. The diagram must clearly identify the lease on which the facility is located and the site security plan to which it is subject along with the location of the plan.

(4) Site facility diagrams submitted under this section will satisfy the requirement for facility diagrams appearing at any other section of this part.

§ 3162.8 Confidentiality.

(a) Information obtained pursuant to this part and on file shall be open for public inspection and copying during regular office hours upon a written request, pursuant to rules at 43 CFR Part 2, except that: (1) Upon request, information obtained from a lessee under this part that constitutes trade secrets and commercial or financial information which is privileged or confidential or other information that may be withheld under the Freedom of Information Act (5 U.S.C. 552(b)), such as geologic and geophysical data and maps, shall not be available for public inspection or made public or disclosed without the consent of the lessee for a period of 12 months; (2) upon expiration of the 12-month period, the lessee may request that the data be held confidential for an additional 12-month period; and (3) upon termination of a lease, whether by expiration of its terms or otherwise, such information shall be made available to the public.

(b) Information requested to be kept confidential under this section shall be clearly identified by the lessee by marking each page of documents submitted with the words "CONFIDENTIAL INFORMATION" at the top of the page. All pages so marked shall be physically separated from other portions of the submitted materials. All information not marked "CONFIDENTIAL INFORMATION" will be available for public inspection.

(c) Confidential and privileged information obtained from a lessee under this part on a restricted Indian lease

shall be available only to the Tribe or allotted Indian lessor, their designated agent, or authorized U.S. Department of the Interior officials. Such information shall not be made available to any other party without the express authorization of the Tribe or allotted Indian lessor.

(d) Any geological, geophysical, or financial information which is either not required under the regulations in this part or covers lands not under Federal or Indian leases, but which the lessee submits to the authorized officer, shall be held confidential and shall not be released without the lessee's consent.

(e) Trade secrets, proprietary and other confidential information obtained pursuant to this part shall be made available to States and Indian Tribes upon their request for the purpose of conducting an investigation if:

(1) Such State or Indian Tribe consents in writing to restrict the dissemination of the information to those who are directly involved in an investigation under a cooperative agreement approved by the Secretary, and who need to know;

(2) Such State or Indian Tribe accepts liability for wrongful disclosure;

(3) In the case of a State, such State demonstrates that such information is essential to the conduct of an investigation or to litigation; and

(4) In the case of an Indian Tribe, such Tribe demonstrates that such information is essential to the conduct of an investigation and waives sovereign immunity by express consent for wrongful disclosure by such Tribe.

(f) The United States shall not be liable for the wrongful disclosure by any individual, State, or Indian Tribe of any information provided to such individual, State, or Indian Tribe pursuant to any cooperative agreement or a delegation.

(g) Whenever any individual, State or Indian Tribe has obtained possession of information pursuant to a cooperative agreement or any individual or State has obtained possession of information pursuant to a delegation of authority, the individual shall be subject to the same provisions of law with respect to the disclosure of such information as would apply to an officer or employee of the United States or of any Department or agency thereof and the State or Indian Tribe shall be subject to the same provisions of law with respect to the disclosure of such information as would apply to the United States or any Department or agency thereof. No State or State officer or employee who receives trade secrets, proprietary information or other confidential information under Title II of the Federal Oil and Gas Royalty Management Act may be required to disclose such information under State Law.

[47 FR 47765, Oct. 27, 1982. Redesignated and amended at 48 FR 36583, 36585, Aug. 12, 1983; 49 FR 37364, Sept. 21, 1984]

Subpart 3163—Noncompliance and Assessments

§ 3163.1 Remedies for acts of noncompliance.

In the event of an act of noncompliance, the authorized officer is authorized to shut down operations; to enter upon a lease and to perform, or have performed, at the sole risk and expense of the lessee, operations that the lessee fails to perform when directed in writing by the authorized officer; to recommend cancellation of the lease and forfeiture under the bond; and to assess penalties and/or liquidated damages in specific instances of noncompliance when the lessee fails to comply with applicable law, the regulations in this part or promulgated under the cited laws, the lease terms, the approved operating plan, or the written orders or instructions issued by the authorized officer.

§ 3163.2 Shutting down operations; lease cancellations.

(a) When necessary for compliance, entry upon the lease to conduct operations and recommendations for lease cancellation and for foreiture under the surety bond will be taken only after the lessee is duly notified in writing. The lessee will be provided a reasonable period of time to either take corrective action or to show why the lease should not be so entered or recommended for cancellation and forfeiture declared under the surety bond.

(b) Immediate shut-in action may be taken where operations are initiated and conducted without prior approval; or where continued operations could result in the loss of revenue, or serious harm to life, property, or the environment; or for repeated instances of noncompliance. Shut-in actions in other situations may only be taken after due notice, in writing, has been given.

§ 3163.3 Assessments for noncompliance.

Certain instances of noncompliance result in loss or damage to the lessor, the amount of which is difficult or impracticable to ascertain. Except where actual losses or damages can be ascertained in an amount larger than that set forth below, the following amounts shall be deemed to cover loss or damage to the lessor from specific instances of noncompliance.

(a) For failure to comply with a written order or instructions of the authorized officer, $250 if compliance is not obtained within the time specified.

(b) For failure to perform any operation ordered in writing by the authorized officer, if said operation is thereafter performed by or through the authorized officer; the actual cost of performance and an additional 25 percent of such amount to compensate the United States for administrative costs.

(c) For failure to obtain approval of an Application for Permit to Drill prior to commencing operations or causing surface disturbance preliminary thereto or for failure to obtain approval before initiating any major departure from a previously approved permit to drill, $250.

(d) For failure to obtain approval of a plan for subsequent well operations before commencing work on a well to redrill, deepen, convert to injection, using any well for gas storage or water disposal, or any other operation requiring prior approval under § 3162.3-2 of this title, $250.

(e) For failure to properly identify a well location or derrick, whether the well is drilling, producing, or abandoned, or a production facility, $100.

(f) For failure to install blowout preventers or other related drilling safety and control equipment as required by the approved drilling plan, $250.

(g) For failure to exercise due care and diligence in preventing undue damage to surface or subsurface resources or surface improvements as required by the regulations in this part and the applicable lease terms, $250.

(h) For failure to maintain records and file required reports, records, samples, or data as required by the regulations in this part and by applicable orders and notices, $100.

(i) For failure to obtain approval of a plan for well abandonment prior to commencement of such operations, $250.

(j) For failure to maintain effective seals required by the regulations in this part and by applicable orders and notices, or for failure to maintain the integrity of any seal placed upon any property or equipment by the authorized officer, $250.

[47 FR 47765, Oct. 27, 1982. Redesignated and amended at 48 FR 36583, 36585, Aug. 12, 1983; 49 FR 37365, Sept. 21 1984]

§ 1363.4-1 Administrative penalties.

(a) *Mineral Leasing Act.* (1) Whenever a lessee fails to comply with any provisions of the lease, the regulations in this part, applicable orders or notices, or any other appropriate orders of the authorized officer, the authorized officer shall give the lessee notice in writing to remedy any defaults or violations.

(2) If there is a failure to complete the necessary remedial action within the time and in the manner prescribed by the notice, the lessee shall be liable for a penalty of not more than $500 per day for each day the violation continues beyond the date specified in the notice through the 20th day of such noncompliance.

(3) A penalty shall be imposed under paragraph (a) of this section for the failure to abate violations which are required to be corrected in less than 20 days from the date of the report or notice.

(4) A notice of proposed penalty shall be issued and served by personal service by an authorized officer or by certified mail. Service shall be deemed to occur when received or 5 days after the date it is mailed, whichever is earlier. Any person may designate a representative to receive any notice on their behalf. Any person authorized by the lessee to submit reports, notices, affidavits, records, or other information required by regulations in this part or who is authorized by the lessee to conduct or supervise operations subject to regulations in this part may receive the notices. If no designation pertaining to that lease has been filed, the notice shall be served as previously described. A person charged with a violation and served with a notice of civil penalty under this paragraph may request a technical and procedural review under § 3165.3

of this title within 10 working days of receipt of the notice. Such review shall be limited to the issues of whether a violation actually existed and, if so, whether the gravity attached to the violation was appropriate, and whether a reasonable abatement period was prescribed. Within 30 days of service of a notice of penalty, or within 15 days of receipt of the decision on the technical and procedural review, whichever is later, the person charged shall either file an appeal pursuant to part 4 of this title or pay the civil penalty.

(b) *Federal Oil and Gas Royalty Management Act.* (1) Whenever a lessee fails or refuses to comply with any applicable requirements of the Federal Oil and Gas Royalty Management Act, any mineral leasing law, any rule or regulation thereunder, or the terms of any lease or permit issued thereunder, the authorized officer shall notify the lessee in writing of the violation, unless the violation was discovered and reported to the authorized officer by the liable person or the notice as previously issued under paragraph (a) of this section. If the violation is not corrected within 20 days of such notice or report, or such longer time as the authorized officer may agree to in writing, the lessee shall be liable for a civil penalty of up to $500 per violation for each day such violation continues, dating from the date of such notice or report. This notice shall be issued and served by personal service by an authorized officer or by certified mail. Service shall be deemed to occur when received or 5 days after the date it is mailed, whichever is earlier.

(2) If the violation specified in paragraph (b) (1) of this section is not corrected within 40 days of such notice or report, or a longer period as the authorized officer may agree to in writing, the lessee shall be liable for a civil penalty of not more than $5,000 per violation for each day the violation continues, not to exceed a maximum of 60 days, dating from the date of such notice or report.

(3) In the event the authorized officer agrees to an abatement period of more than 20 days, the date of notice

shall be deemed to be 20 days prior to the end of such longer abatement period for the purpose of civil penalty calculation.

(4) Whenever a transporter fails to permit inspection of proper documentation by any authorized representative, as provided in § 3162.7-1(c) of this title, the transporter shall be liable for a civil penalty of up to $500 per day for the violation, not to exceed a maximum of 20 days, dating from the date of notice of the failure to permit inspection and continuing until the proper documentation is provided.

(5) Any person who:

(i) Fails or refuses to permit lawful entry or inspection authorized by § 3162.1(b) of this title; or

(ii) Knowingly or willfully fails to notify the authorized officer by letter or Sundry Notice, Form 3160-5, or orally to be followed by a letter or Sundry Notice, not later than the 5th business day after any well begins production on which royalty is due, or resumes production in the case of a well which has been off of production for more than 90 days, from a well located on a lease site, or allocated to a lease site, of the date on which such production began or resumed; shall be liable for a civil penalty of up to $10,000 per violation for each day such violation continues, not to exceed a maximum of 20 days.

(6) Any person who:

(i) Knowingly or willfully prepares, maintains or submits false, inaccurate or misleading reports, notices, affidavits, records, data or other written information required by this part; or

(ii) Knowingly or willfully takes or removes, transports, uses or diverts any oil or gas from any Federal or Indian lease site without having valid legal authority to do so; or

(iii) Purchases, accepts, sells, transports or conveys to another any oil or gas knowing or having reason to know that such oil or gas was stolen or unlawfully removed or diverted from a Federal or Indian lease site; shall be liable for a civil penalty of up to $25,000 per violation for each day such violation continues, not to exceed a maximum of 20 days.

(7) (i) Notice of violation imposed by the authorized officer under this section shall be by personal service or by certified mail. Any person may designate a representative to receive any notice on their behalf. Any person who is authorized by the lessee to submit reports, notices, affidavits, records data or other information required by this part or who is authorized by the lessee to conduct or supervise operations subject to regulations in this part may receive the notices. If no designation has been filed, the notice shall be served as previously described.

(ii) A person charged with a violation and served with a notice of civil penalty may request a technical and procedural review under § 3165.3 of this title within 10 working days of receipt of the notice. Such review shall be limited to the issues of whether a violation actually existed and, if so, whether the gravity attached to the violation was appropriate, and whether a reasonable abatement period was prescribed. Within 30 days of service of a notice of penalty, or within 15 days of receipt of the decision on the technical and procedural review, whichever is later, the person charged shall either request a hearing on the record or pay the civil penalty. A request for a hearing shall be filed within the time allowed in the office of the State Director having jurisdiction of the lands covered by the lease. No civil penalty shall be assessed under this section until the person charged with the violation has been given the opportunity for a hearing on the record under Part 4 of this title.

(8) On a case-by-case basis, the Secretary may compromise or reduce civil penalties under paragraph (b) of this section. In compromising or reducing the amount of a civil penalty under paragraph (b) of this section, the Secretary shall state on the record the reasons for his/her determinations.

(9) Any person who has requested a hearing in accordance with paragraph (b) (7) of this section and who is aggrieved by a final order of the Secretary under this section may seek review of such order in the United States District Court for the judicial district in which the alleged violation occurred. Review by the district court shall be on the administrative record only and not de novo. Such an action shall be barred unless filed within 90 days after the Secretary's final order.

(10) Civil penalties provided by this section shall be supplemental to, and not in derogation of, any other penalties or assessment for noncompliance in any other provision of law.

(11) If the violation continues beyond the 60-day maximum specified in paragraph (b) (2) of this section or beyond the 20-day maximum specified in paragraphs (b) (5) and (b) (6) of this section, lease cancellation proceedings shall be initiated under either Title 43 or Title 25 of the Code of Federal Regulations.

(12) If the violation continues beyond the 20-day maximum specified in paragraph (b) (4) of this section, the District Manager shall revoke the transporter's authority to remove crude oil or other liquid hydrocarbons from any Federal or Indian lease under the authority of that District Manager or to remove any crude oil or liquid hydrocarbons allocated to such lease site. This revocation of the transporter's authority shall continue until compliance is achieved and the related penalty paid.

(c) If any person fails to pay an assessment of a civil penalty under paragraph (b) of this section after the

order making the assessment has become a final order, and if such person does not file a petition for judicial review in accordance with this subpart, or, after a court in an action brought under this subpart has entered a final judgment in favor of the Secretary, the court shall have jurisdiction to award the amount assessed plus interest from the date of the expiration of the 90-day period provided by paragraph (b)(9) of this section. Judgment by the court shall include an order to pay.

(d) The common drilling, production and abandonment related violations are categorized into 3 noncompliance ranges. The category for any violation is the gravity level to be used for that violation. Based on individual circumstances and with the appropriate documentation, the gravity of a violation may be upgraded or downgraded by 1 level. The Director shall establish a detailed list of potential violations. The violations shall be either:

(1) A minor violation which does not affect the safety of the workplace, nor does it degrade the environment or affect the amount of royalty income; or

(2) A moderate violation, which if left uncorrected, may eventually affect the safety of the workplace, degrade the environment and/or affect royalty income; or

(3) A major violation which has the immediate potential to affect the safety of the workplace, degrade the environment and/or affect the royalty income.

(e) Determination of Penalty Amount for paragraphs (a) and (b) of this section are as follows:

(1) The amount of the administrative penalty proposed shall be based upon the formula set forth in this subsection. The formula is based on 2 criteria: i.e., the gravity of the violation; and the lessee's or transporter's history of previous violations;

(2) The appropriate number of penalty points shall be assigned to each criterion using the appropriate tables as denoted and the 2 numbers shall then be totaled, and the point accumulation converted into a dollar per day amount by using Penalty Conversion Table A, B, C or D, as appropriate, and the amounts added, if necessary.

(3) Table I—Gravity of the Violation:

Classification	Penalty points
Minor violations	11
Moderate violations	41
Major violations	71

(4) Table II—Lessee's or Transporter's History of Past Violations:

Minor violations ..... Number × ½ = ...
Moderate violations ..... Number × 2 = ...
Major violations ..... Number × 5 = ...

Total—(rounded down to the nearest whole number) (maximum of 29).

History of previous violations standards. History is based on the number of violations issued in a preceding 36-month period beginning February 1, 1983. The history of previous violations may account for a maximum of 29 penalty points. The penalty points shall be calculated on a lessee-by-lessee and lease-by-lease basis and, in the case of transporters, on a transporter-by-transporter basis within the jurisdictional area of each Bureau of Land Management District Office.

(5) Penalty Conversion Table—A (Lessees):

(i) The following penalty conversion tables are for violations not corrected within the time allowed in paragraph (a) of this section, or by the 20th day under paragraph (b) (1) of this section, or by the 40th day under paragraph (b) (2) of this section or such other

time period as the authorized officer may specify and shall be used to convert the accumulation of penalty points from Tables I and II above to the appropriate dollar per day proposed penalty.

PENALTY CONVERSION TABLE—A

Points	Not corrected for up to 40 days-penalty/dollars per day under paragraph (a) and/or (b)	Not corrected 40 days—penalty/dollars per day
40	75	750
41	79	790
42	82	820
43	86	860
44	89	890
45	93	930
46	97	970
47	101	1,010
48	105	1,050
49	109	1,090
50	113	1,130
51	117	1,170
52	122	1,220
53	126	1,260
54	131	1,310
55	135	1,350
56	140	1,400
57	145	1,450
58	150	1,500
59	156	1,560
60	160	1,600
61	166	1,660
62	171	1,710
63	177	1,770
64	182	1,820
65	188	1,880
66	194	1,940
67	200	2,000

PENALTY CONVERSION TABLE—A—Continued

Points	Not corrected for up to 40 days-penalty/dollars per day under paragraph (a) and/or (b)	Not corrected 40 days—penalty/dollars per day
68	206	2,060
69	212	2,120
70	218	2,180
71	225	2,250
72	233	2,330
73	243	2,430
74	250	2,500
75	258	2,580
76	266	2,660
77	274	2,740
78	282	2,820
79	290	2,900
80	298	2,980
81	306	3,060
82	315	3,150
83	323	3,230
84	332	3,320
85	340	3,400
86	349	3,490
87	358	3,580
88	367	3,670
89	376	3,760
90	385	3,850
91	395	3,950
92	405	4,050
93	415	4,150
94	425	4,250
95	435	4,350
96	448	4,480
97	461	4,610
98	474	4,740
99	487	4,870
100	500	5,000

(ii) In order to focus particularly on serious violations, while also considering an operator's past compliance history, no dollar penalty shall be proposed for violations totaling less than 40 penalty points.

(6) Penalty Conversion Table A (Transporters):

The amount of the proposed civil penalty for failure of a transporter to permit inspection of proper documentation required by paragraph (b)(4) of this section shall be determined by formula based on the following criteria: i.e., the violation shall be considered a major violation (see Table I); and the transporter's history of previous violations shall be assigned to each criterion and the 2 numbers shall then be totaled, and the point accumulation converted to a dollar per day amount by using the first column of "Penalty Conversion Table A".

(7) Penalty Conversion Table (B):

(i) The amount of the proposed civil penalty for violation of paragraph (b)(5) of this section shall be determined by the formula based on the following criteria: i.e., the specific violation (Table III); and the lessee's history of previous violations (Table II).

(ii) Penalty points shall be assigned to each criterion and the 2 numbers shall then be totaled, and the point accumulation converted to a dollar per day amount by using "Penalty Conversion Table B."

TABLE III—TYPE OF VIOLATION

Violation	Penalty points
Fail to permit entry upon the leasehold	70
Fails to permit inspection	60
Knowingly or willfully fails to notify after well begins or resumes production by the 5th business day thereafter	65

(iii) The following penalty conversion table shall be used to convert the accumulation of penalty points from Tables II and III to the appropriate per day proposed monetary penalty.

PENALTY CONVERSION TABLE—B

Points	Penalty dollars per day
60	3,600
61	3,720
62	3,840
63	3,970
64	4,100
65	4,220
66	4,360
67	4,490
68	4,620
69	4,760
70	4,900
71	5,040
72	5,180
73	5,330
74	5,480
75	5,630
76	5,780
77	5,930
78	6,080
79	6,240
80	6,400
81	6,560
82	6,720
83	6,890
84	7,060
85	7,220
86	7,400
87	7,570
88	7,740
89	7,920

90	8,100
91	8,280
92	8,460
93	8,650
94	8,840
95	9,030
96	9,220
97	9,410
98	9,600
99	9,800
100 and above	10,000

(8) Penalty Conversion Table—C:

(i) The amount of the proposed civil penalty for violations of paragraph (b)(6) of this section shall be determined by the formula based on the following criteria: i.e., the specific violation (Table IV); and the lessee's history of previous violations (Table II).

(ii) Penalty points shall be assigned to each criterion and the 2 numbers shall then be totaled, and the point accumulation converted to a dollar per day amount by using "Penalty Conversion Table—C."

TABLE IV—TYPE OF VIOLATION

Violation	Penalty points
Knowingly or willfully prepares, maintains or submits false or misleading written information	70
Knowingly or willfully prepares, maintains or submits inaccurate written information	60
Knowingly or willfully removes, uses or diverts oil or gas from any lease without having legal authority to do so	70
Purchases, accepts, sells, transport or conveys to another any oil or gas knowing or having reason to know that such oil or gas was stolen or unlawfully removed or diverted	70

(iii) The following penalty conversion table shall be used to convert the accumulation of penalty points from Tables II and IV to the appropriate per day proposed monetary penalty.

PENALTY CONVERSION TABLE—C

Points	Penalty dollars per day
60	9,000
61	9,300
62	9,600
63	9,925
64	10,250
65	10,550
66	10,900
67	11,225
68	11,550
69	11,900
70	12,250
71	12,600
72	12,950
73	13,325
74	13,700
75	14,075
76	14,450
77	14,825
78	15,200
79	15,600
80	16,000
81	16,400
82	16,800
83	17,225
84	17,650
85	18,050
86	18,500
87	18,925
88	19,350
89	19,800

90	20,250
91	20,700
92	21,150
93	21,625
94	22,100
95	22,575
96	23,050
97	23,525
98	24,000
99	24,500
100 and above	25,000

[49 FR 37365, Sept. 21, 1984]

§ 3163.4-2 Criminal penalties.

Any person who commits an act for which a civil penalty is provided in § 3163.4-1(b)(6) of this title shall, upon conviction, be punished by a fine of not more than $50,000 or by imprisonment for not more than 2 years or both.

[49 FR 37367, Sept. 21, 1984]

§ 3163.5 Assessments and administrative penalties.

(a) Assessments made under § 3163.3 of this title are due upon issuance and shall be paid within 30 days of receipt of certified mail written notice or personal service, as directed by the authorized officer in the notice. Failure to pay assessed damages timely will be subject to late payment charges as prescribed under Title 30 CFR Group 202.

(b) Administrative penalties under § 3163.4-1 of this title shall be paid within 30 days of completion of any final order of the Secretary or the final order of the Court.

(c) Payments made pursuant to this section shall not relieve the lessee from the responsibility of compliance

with the regulations in this part or from liability for waste or any other damage. A waiver of any particular assessment shall not be construed as precluding an assessment pursuant to § 3163.3 of this title for any other act of noncompliance occurring at the same time or at any other time. The amount of any civil penalty under § 3163.4-1(b) of this title, as finally determined may be deducted from any sums owing by the United States to the person charged.

[47 FR 47765, Oct. 27, 1982. Redesignated and amended at 48 FR 36583, 36586, Aug. 12, 1983; 49 FR 37368, Sept. 21, 1984]

§ 3163.6 Injunction and specific performance.

(a) In addition to any other remedy under this part or any mineral leasing law, the Attorney General of the United States or his designee may bring a civil action in a district court of the United States to:

(1) Restrain any violation of the Federal Oil and Gas Royalty and Management Act or any mineral leasing law of the United States; or

(2) Compel the taking of any action required by or under the Act or any mineral leasing law of the United States.

(b) A civil action described in paragraph (a) may be brought only in the United States district court of the judicial district wherein the act, omission or transaction constituting a violation under the Act or any other mineral leasing law occurred, or wherein the defendant is found or transacts business.

[49 FR 37368, Sept. 21, 1984]

Subpart 3164—Special Provisions

§ 3164.1 Onshore Oil and Gas Orders.

(a) The Director is authorized to issue Onshore Oil and Gas Orders when necessary to implement and supplement the regulations in this part. All orders will be published in the FEDERAL REGISTER both for public comment and in final form.

(b) These Orders are binding on lessees and operators of Federal and restricted Indian oil and gas leases which have been, or may hereafter be, issued. The Onshore Oil and Gas Orders listed below are currently in effect:

Order No.	Subject	Effective date	FEDERAL REGISTER reference	Supersedes
1	Approval of operations.	November 12, 1983	48 FR 48916, and 48 FR 56226.	NTL-6.

[47 FR 47765, Oct. 27, 1982. Redesignated at 48 FR 36583, Aug. 12, 1983, and amended at 48 FR 48921, Oct. 21, 1983; 48 FR 56226, Dec. 20, 1983]

§ 3164.2 NTL's and other implementing procedures.

(a) The authorized officer is authorized to issue NTL's when necessary to implement the onshore oil and gas orders and the regulations in this part. All NTL's will be issued after notice and opportunity for comment.

(b) All NTL's issued prior to the promulgation of these regulations shall remain in effect until modified, superseded by an Onshore Oil and Gas Order, or otherwise terminated.

(c) A manual and other written instructions will be used to provide policy and procedures for internal guidance of the Bureau of Land Management.

§ 3164.3 Surface rights.

(a) Lessees shall have the right of surface use only to the extent specifically granted by the lease. With respect to restricted Indian lands, additional surface rights may be exercised when granted by a written agreement with the Indian surface owner and approved by the Superintendent of the Indian agency having jurisdiction.

(b) The authorized officer is responsible for approving and supervising the surface use of all drilling, development, and production activities on the leasehold. This includes storage tanks and processing facilities, sales facilities, all pipelines upstream from such facilities, and other facilities to aid production such as water disposal pits and lines, and gas or water injection lines.

§ 3164.4 Damages on restricted Indian lands.

Assessments for damages to lands, crops, buildings, and to other improvements on restricted Indian lands shall be made by the Superintendent and be payable in the manner prescribed by said official.

Subpart 3165—Relief, Conflicts, and Appeals

§ 3165.1 Relief from operating and producing requirements.

(a) Applications for relief from either the operating or the producing requirements of a lease, or both, shall be filed in triplicate with the authorized officer, and they shall include a full statement of the circumstances that render such relief necessary.

(b) The authorized officer, in the interest of conservation, is authorized to act on applications submitted for a suspension of operations or production or both filed pursuant to 43 CFR Subpart 3103. The application for suspension must be filed with the authorized officer prior to the expiration data of the lease; must be executed by all lessees of record or, in the case of a Federal unit ap-

proved under Part 3180 of this title, by the unit operator on behalf of committed tracts or by all lessees of such tracts; and include a full statement of the circumstances that render such relief necessary.

(c) If approved, a suspension of operations and production will be effective on the first of the month in which the completed application was filed with the authorized officer. Suspensions will terminate when they are no longer justified in the interest of conservation, when such action is in the interest of the lessor, or as otherwise stated by the authorized officer in the approval letter.

§ 3165.1-1 Relief from royalty and rental requirements.

Applications for any modification authorized by law of the royalty or rental requirements of a lease for lands of the United States shall be filed in triplicate in the office of the authorized officer having jurisdiction of the lands. (For other regulations relating to royalty and rental relief, and suspension of operations and production, see Part 3103 of this title.)

[48 FR 36586, Aug. 12, 1983]

§ 3165.2 Conflicts between regulations.

In the event of any conflict between the regulations in this part and the regulations in Title 25 CFR concerning oil and gas operations on Federal and Indian leaseholds, the regulations in this part shall govern with respect to the lessee's obligations in the conduct of oil and gas operations, acts of noncompliance, and the jurisdiction and authority of the authorized officer.

§ 3165.3 Technical and procedural review.

A lessee or operator may request a technical and procedural review of any instructions, orders, or decisions issued by the authorized officer under the regulations in this part. Such request including all supporting documentation must be filed in writing within 10 working

days of the date such instructions, orders, or decisions were received and must be filed with the appropriate State Director. Such a request shall not result in a suspension of the instruction or order unless the reviewing official so determines. The reviewing official will issue a final decision within 10 working days. Where a technical and procedural review is requested, the decision issued upon review will represent the final decision from which an appeal may be taken pursuant to § 3165.4 of this title.

§ 3165.4 Appeals.

Instructions, orders or decisions issued under the regulations in this part may be appealed in accordance with the provisions of Part 4 of this title if Federal lands are involved or 25 CFR Part 2 if Indian lands are involved. An appeal shall not result in a suspension of the requirement for compliance with the order or decision from which the appeal is taken unless the official to whom the appeal is made determines that suspension of the requirements of the order or decision will not be detrimental to the interests of the lessor or upon submission and acceptance of a bond deemed adequate to indemnify the lessor from loss or damage.

[48 FR 36586, Aug. 12, 1983]

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Wednesday, February 5, 1986
Proposed Rules

P. 4507

DEPARTMENT OF THE INTERIOR

Minerals Management Service

30 CFR Parts 202, 203, 206, and 212

Product Valuation for Royalty Purposes

AGENCY: Minerals Management Service (MMS), Interior.

ACTION: Advance notice of proposed rulemaking.

SUMMARY: The Minerals Management Service (MMS) hereby gives notice that it is making available for public comment drafts of proposed methods of valuing, for royalty purposes, coal, oil, and gas and associated products from Federal and Indian leases. MMS is making these drafts available to obtain initial public comment on specific proposed methods before it formally issues proposed regulations.

DATES: Comments must be received on or before April 7, 1986. A public meeting will be held on March 18 and 19, 1986, at 8:30 a.m. to 4:00 p.m.

ADDRESSES: Comments should be mailed to Minerals Management Service, Royalty Management Program, Office of External Affairs, Denver Federal Center, Building 85, P.O. Box 25165, Mail Stop 660, Denver, Colorado 80225, Attention: Vernon B. Ingraham. Copies of the draft regulations may be obtained from the above address. The public meeting will be held at the Denver Federal Center, Building 25, Room 1254, Lakewood, Colorado 80225.

FOR FURTHER INFORMATION CONTACT: Vernon B. Ingraham, telephone: (303) 231-3360, (FTS) 326-3360.

SUPPLEMENTARY INFORMATION:

I. Background

Regulations governing the valuation for royalty purposes of coal, oil, and gas and associated products from Federal and Indian leases are codified in various sections of Title 30 and 43 of the Code of Federal Regulations. In addition, other regulatory and related provisions are included in various Notices to Lessees and orders.

For the past several months, MMS has been reviewing the existing regulatory scheme for royalty valuation and developing proposals for new methods for valuation which would simplify, clarify, and consolidate the existing provisions. In furtherance of the effort to develop comprehensive and workable product value regulations, the Secretary of the Interior recently Royalty Management Advisory Committee comprised of 31 representatives from industry, the states and Indian Tribes, which will have as one of its first tasks to advise the Secretary on the new product value regulations. The Advisory Committee held its first meeting in Lakewood, Colorado on January 9 and 10, 1986.

II. Draft Regulations

As a result of its extensive review and consideration of royalty valuation issues, MMS has developed draft regulations for product valuation. There are five separate draft regulations; coal, oil, gas and associated products, gas processing allowances, and transportation allowances. Each draft is in the form of a notice of proposed rulemaking, including proposed regulatory language and a preamble.

Because the issues related to product valuation are so complex, and because MMS expects extensive public comment, it has decided to make drafts of the proposed regulations available for public review and comment before issuing formal Notices of Proposed Rulemaking. The

existing draft regulations reflect MMS current proposals for addressing product valuation but we expect that changes will be made as a result of comments before proposed rules are issued.

Commenters are specifically requested to provide alternative suggestions to those specified in the draft rules. In addition, a public meeting will be held for the purpose of receiving comments at the time and location stated in the DATES and ADDRESSES sections. All written comments, plus comments received at the public meeting, will be made available to the Royalty Management Advisory Committee for its consideration in providing advice to the Secretary of the Interior on product valuation.

Although each of the five drafts is in the form of a proposed rule, MMS is not considering them as proposed rules at this time and the proposed rules will be published in the Federal Register for public comment before final rules are issued.

III. Availability of Draft Regulations

At this time, only four of the five draft regulatory packages are being made available for comments: coal, oil, gas processing allowances and transportation allowances. The draft rule for gas and associated products will be available in a few weeks and MMS will send copies to those requesting them at that time. Interested persons may obtain a copy of the draft regulations upon request from the MMS at the address above in ADDRESSES.

[4310-MR] DRAFT Feb. 7, 1986

DEPARTMENT OF THE INTERIOR

Minerals Management Service

30 CFR Parts 202, 206, and 207

Revision and Gas and Associated Products Royalty Valuation Regulations and Related Topics

AGENCY: Minerals Management Service (MMS), Department of the Interior (DOI)

ACTION: Proposed Rulemaking

SUMMARY: This proposed rulemaking provides for the amendment and clarification of regulations governing valuation of gas and associated products for royalty computation purposes. The amended and clarified regulations govern the methods b, which value is determined when computing gas and associated products royalties and net profit shares under Federal (onshore and Outer Continental Shelf) and Indian (tribal and allotted) oil and gas leases (except leases on the Osage Indian Reservation, Osage County, Oklahoma).

DATES: The comment period on this proposed rulemaking will remain open until further notice published in the FEDERAL REGISTER. Hearing dates: (To be determined prior to publication).

ADDRESSES: Written comments may be mailed to Mr. William H. Feldmiller, Royalty Management Program, Royalty Valuation and Standards Division, Mail Stop 653, P.O. Box 25165, Denver, Colorado 80225.

Hearing Locations: (To be determined).

FOR FURTHER INFORMATION CONTACT: Mr. John L. Price (303) 231-3392, (FTS) 326-3392; Mr. Scott Ellis (303) 231-3543, (FTS) 326-3543; Mr. Thomas J. Blair (303) 231-3153 (FTS) 326-3153; or Mr. William H. Feldmiller (303) 231-3184, (FTS) 326-3184 in Lakewood, Colorado.

SUPPLEMENTARY INFORMATION: The principal authors of this rulemaking are John L. Price, Scott Ellis, Thomas J. Blair, William H. Feldmiller.

I. Purpose and Background

The Minerals Management Service (MMS) is proposing to revise the current regulations regarding the valuation of gas and associated products to accomplish the following:

(1) Clarification and reorganization of the existing regulations at 30 CFR Parts 202, 206, and 207.

(2) Creation of regulations consistent with the present organizational structure of the Department of the Interior. The existing onshore valuation regulations were implemented when royalty valuation for gas and associated products was the function of an organization that is now part of the Bureau of Land Management (BLM).

(3) Placement of the gas and associated products royalty valuation regulations in a format that will be compatible with the valuation regulations for all leasable minerals.

(4) Clarification that royalty is to be paid on take-or-pay payments and tax reimbursements, as well as on other consideration received by lessees as gross proceeds.

In addition to the items listed above, these proposed regulations also would clarify policy on the following issues:

(1) Royalty would be based on the price received by the lessee under its arm's-length contract.

(2) Prices received by the lessee under its non-arm's-length contract would be accepted as the basis for gas, principal products and associated products value for royalty purposes if the lessee can demonstrate to MMS that the price obtained thereunder is similar to that in arm's-length contracts in the same field or area for like-quality gas, principal products and associated products.

(3) In the absence of an arm's-length contract in the same field or area, a prioritized benchmark system would be used in establishing value for royalty purposes.

A number of sections would be renumbered and/or moved to a new subpart. In addition, §§ 202.152, 206.150, 206.151, 206.152, 206.153, 206.154, and 207.150 were added to the appropriate subparts.

This proposed rule is to be applied prospectively. It would supersede all existing gas and associated products royalty valuation directives contained in numerous Secretarial, Minerals Management Service (MMS), and the U.S. Geological Survey Conservation Division (now Bureau of Land Management, Onshore Operations Division) directives, regulations and NTL's (Notice to Lessees) issued over past years. Specific guidelines governing the application of the gas and associated products valuation regulations will be incorporated into the MMS Payor Handbook subsequent to the issuance of this rulemaking in the Federal Register.

For the convenience of oil and gas lessees, payors and the public, the following chart summarizes the effects of these proposed rules.

REGULATION CHANGES	DESCRIPTIONS
I. REDESIGNATIONS:	
1. Sections 206.105, and 206.106 are redesignated as §§ 202.150, and 202.151, respectively.	This administrative action more appropriately locates within 30 CFR the information contained in these sections.
II. DELETIONS:	
1. Section 206.107 is deleted from Subpart B of Part 206.	This section has been incorporated into Section 202.100.
III. ADDITIONS	
1. Section 202.152 is added to Part 202. Sections 206.150, 206.151, 206.152, 206.153 and 206.154 are added to Part 206.	These new sections provide gas, principal products and associated products valuation standards and procedures.
2. Section 207.150 is added to Part 207.	This new section will set forth certain recordkeeping requirements.

These proposed rules would apply the same valuation standards to gas, principal products and associated products produced on Indian lands and gas, principal products and associated products produced on Federal lands. It is appropriate to use the same criteria for product valuation on Indian and Federal leases for several reasons. Establishing a comprehensive and reasonable royalty valuation policy satisfies the Secretary's responsibility as trustee for the Indians in the administration of their leases. Also, it provides consistency and limits confusion for the lessees.

The proposed method of valuation for royalty purposes would yield a result which is consistent with MMS' responsibility on Indian leases. The basic premise underlying the method is that the value is best determined by the interaction of competing market forces. Because the proposed valuation method would secure for the Indians and the Federal government a fair and just return from oil and gas leasing activities, it obviates the need to treat Indian lands differently from Federal lands.

Prior to the promulgation of these proposed gas and associated products royalty valuation regulations, the MMS promulgated proposed regulations entitled "Revisions of Coal Royalty Valuation Regulations and Related Topics", —— Fed. Reg. ——, ——, 1986. Included in that proposed rulemaking was a definitions section applicable to the royalty valuation of several lease products including gas, principal products and associated products. Commenters should consult the proposed definitions to consider those applicable to gas, principal products and associated products together with this proposed rule. Additional regulations governing the computation of transportation deductions from the value of oil, gas, principal products and associated products and other minerals are proposed to be promulgated subsequent to the gas and associated products royalty valuation regulations.

Prior to the promulgation of these proposed gas and associated products royalty valuation regulations, the MMS promulgated proposed regulations entitled "Revisions of Oil Royalty Valuation Regulations and Related Topics", —— Fed. Reg. ——, ——, 1986. Included in that proposed rulemaking were "General Provisions" for Parts 202, 206 and 207 applicable to oil, gas, principal products and associated products. Commenters should consult those proposed regulations to consider those provisions applicable to gas, principal products and associated products together with this proposed rule.

II. Section-by-Section Analysis

Proposed § 206.5, Definitions, was proposed together with the coal valuation regulations and included definitions applicable to the proposed gas and associated products valuation regulations. Because the comment period on that rulemaking will remain open for an extended period of time, commenters should comment at this time on definitions applicable to the gas and associated products valuation regulations. Most of the proposed definitions applicable to gas and associated products are straightforward and self explanatory. A few of the definitions, however, require further explanation:

"Lessee" would be defined as any person to whom the United States, an Indian tribe, or an Indian allottee, issues a lease, and any person who has been assigned an obligation to make royalty or other payments required by the lease. This is the same definition used in the Federal Oil and Gas Royalty Management Act of 1982, 30 U.S.C. § 1701(7). MMS is proposing to use this definition for the product value regulations because it includes all persons who may have to make royalty payments. This would include all persons who have an interest in a lease as well as an operator or other payor who has a royalty payment responsibility by contract or other agreement with the persons who have the actual lease inter-

ests. By using this broad definition for the product value regulations, it would not be necessary to use multiple terms such as lessee/payor/operator throughout the rules. This definition is not intended to change any contractual obligations under the lease instrument between the lessor and the persons to whom the lease was issued, except as it pertains to royalty valuation.

"Like-quality lease products" would be defined as lease products which have similar chemical, physical, and in the case of hydrocarbon gases, legal characteristics. This definition is required in order to apply valuation standards at § 206.151 and § 206.152 in non-arm's-length or no contract situations where the use of the first criterion to determine value is required. Similar lease product properties are necessary when using the criterion of comparing the value of products produced off the lease to the production in question. A sweet gas with a high heating value (Btu content) cannot be compared favorably with a sour gas with a low heating value. In some cases, the latter example might not even have a market to provide a value. The legal characteristics for hydrocarbon gases primarily refers to the category for which the gas qualifies in accordance with the NGPA of 1978. When determining value of hydrocarbon gases, MMS would not mix NGPA categories of gas.

"Associated products" are defined as all plant products other than the principal product produced by a processing plant. "Principal product" is defined as the product of most economic value which remains at the end of processing. "Gas" is defined as any fluid, either combustible or noncombustible, hydrocarbon or nonhydrocarbon, which is extracted from a reservoir and which has neither independent shape nor form, but tends to expand indefinitely. It is a substance that exists in a gaseous or rarefied state under standard temperature and pressure conditions.

These three definitions are used either separately or together throughout the proposed gas and associated prod-

ucts valuation regulations. Traditionally, the valuation regulations were written to deal primarily with hydrocarbon gas streams. This was especially true when dealing with processed gas. In the last decade, the existing regulations proved difficult to administer when handling gas mixtures of diverse content. Gas plants have been constructed to process gas mixtures where the principal product may not be a hydrocarbon gas. In order to accommodate processing plants that process and sell non-hydrocarbon production, MMS proposes that the regulations utilize terms that encompass this diverse production. The term "gas" will commonly apply to that wellhead mixture as produced. The term "principal product", in the majority of cases, will refer to gas consisting principally of methane, or residue gas. It may also, however, refer to carbon dioxide, sulphur, or any other product by definition. The term "associated products" will refer to natural gas liquids collectively (ethane, propane, butane, pentane, etc.) and other products also produced by a processing plant (carbon dioxide, nitrogen, and sulphur). Allowable processing deductions apply only against individual associated products.

Proposed § 202.150, Royalty on gas, would set forth general policies regarding what gas is subject to royalty. Proposed § 202.150(a) states that royalty must be paid in value unless the Department of the Interior requires payment in-kind. Proposed § 202.150(b) states that all gas is subject to royalty except gas wasted or lost which BLM or MMS, as appropriate, has determined was unavoidably lost, or gas that is used on, or for the benefit of, the lease. Accordingly, royalty would be due on gas avoidably lost as determined by BLM or MMS for onshore and offshore oil and gas operations, respectively. These proposed regulations would eliminate the requirement that the compensation due the lessor for avoidably lost gas be 100 percent of the value of the avoidably lost gas. This is consistent with section 308 of the Federal Oil and Gas Management Act of 1982 (30 U.S.C. 1756).

Gas used for the benefit of a lease, which is royalty free, includes gas used in lease equipment on communitized areas or unit areas when the lease is committed to a communitization agreement or unitization agreement.

Proposed § 202.151, Royalty on processed gas, would require the payment of royalty on the principal product and the associated products resulting from processing gas. Proposed § 202.151(a) would provide for a deduction from royalty payments for the reasonable actual costs of processing the royalty portion of the gas. Proposed § 202.151(b) would provide that royalty would not be due on the principal product or any associated product used in a manner to benefit the lease as provided previously for gas (see § 202.150(b)).

Proposed § 202.152, Standards for reporting and paying royalties on gas, principal products and associated products, would set forth the criteria for reporting volumes of gas, principal products and associated products on which royalty is due.

Proposed § 206.151 and § 206.152 would set forth the standards by which MMS would establish values for royalty purposes for unprocessed gas and processed gas, respectively. Valuation standards have been proposed for each for clarity and to recognize the numerous commodities that result from processing gas which must be valued individually.

In both of these proposed sections, references are made to arm's-length contracts for the sale of gas prior to processing which contain a provision reserving to the lessee the right to process gas. MMS recognizes this feature of gas sales agreements, and where such processing rights are exercised, MMS proposes to treat these contracts under the provisions for processed gas.

Proposed § 206.151(a) would provide for the acceptance by MMS of gross proceeds accruing, or which could accrue, to the lessee under an arm's-length sales contract

as the value of unprocessed gas for royalty purposes. However, if the sales point under the arm's-length contract is different from the point of royalty settlement approved by BLM or MMS, as appropriate, it is proposed that the gross proceeds would be increased for the differences in the quantity and/or quality of the gas between the two points. For example, a lessee is required to measure its gas production for royalty purposes at a meter on the lease. The lessee's arm's-length contract provides for delivery to the purchaser at a point away from the lease. For whatever reason, the volume of gas measured at the point of delivery under the arm's-length contract is less than the volume of gas measured at the approved point of royalty settlement. In this situation, the gross proceeds accruing to the lessee under its arm's-length contract would be increased, for royalty purposes, to reflect the difference in the volumes measured at the two points. This increase, for royalty purposes, would be accomplished by multiplying the volumetric difference times the unit price at which the gas was actually sold. This section would not apply to those situations where the lessee's arm's-length contract, includes a provision reserving to the lessee the right to process the gas and the lessee exercises that right. In such an event, valuation would be governed by § 206.152, which applies to processed gas.

Proposed § 206.151(b) would require MMS' determination of all values for royalty purposes when sales are not pursuant to an arm's-length contract. Under proposed § 206.151(b)(2), MMS would approve, as value for royalty purposes, the gross proceeds accruing, or which could accrue, to the lessee under a non-arm's-length contract if the lessee demonstrated that its contract was similar to arm's-length contracts. The contract itself does not become, and is not regarded as, an arm's-length contract; rather, the value specified thereunder would be acceptable for royalty purposes as if it were arm's-length. This valuation method could not be used for a non-arm's-length contract unless MMS expressly so determines.

If the disposition of unprocessed gas, from a Federal or Indian lease is not pursuant to an arm's-length contract, or a non-arm's-length contract that would be treated, for royalty valuation purposes, as an arm's-length contract, then the MMS would approve reasonable valuation proposals using certain criteria. This valuation process would be used in the following circumstances: there is no contract for the sale of gas; gas is sold or used in its entirety intra-company; or gas is avoidably lost or for any reason improperly disposed of without sale.

In these situations, § 206.151(b)(3) of the proposed regulations would require that MMS must determine the value through application of criteria in a prescribed order. In other words, the second criterion would not be considered unless the first criterion could not reasonably be applied. Likewise, the third and fourth criteria would not be considered unless those preceding it were not applicable, etc.

MMS is proposing to use as the first criterion prices being paid for similar-sized quantities of like-quality gas from the same field (or if there is no arm's-length contract for the same field, then a field as near the lease as possible) under representative, recently executed arm's-length contracts. This method was selected because it provides the best measure of the value of the gas if it were to be made available for sale today. It will be used where there is an array of comparable sales contracts, and leaves some discretion to MMS to select a value based on the most recent arm's-length contracts. MMS believes this method is preferable to the major portion analysis provided for in existing oil and gas regulations which proved difficult to administer. See 30 CFR § 206.103. If the first valuation criterion is inapplicable to a particular situation, the second criterion applied would be price postings applicable to gas from the same field (or if there is no price posted for gas from the same field, then a field as near the lease as possible).

In the event that there are no postings which are applicable to a particular valuation situation, spot price postings as near the lease as possible would be implemented as the third criterion. MMS believes that these prices are the next best indicator of the value of gas. Should there be no spot price postings which are applicable, the fourth criterion, gas prices reported to the Federal Energy Regulatory Commission (FERC) or the Energy Information Administration (EIA), for that gas would be implemented. MMS believes that these gas prices reported to the Department of Energy regulatory agencies are indicators of the value of gas, and would be acceptable as value for royalty purposes.

If the first four criteria are not appropriate, MMS will utilize information submitted by the lessee concerning circumstances unique to a particular lease operation. MMS would afford the lessee the opportunity to demonstrate to MMS, through the submittal of supporting documents, why the prices contained in its proposal should be used as value for royalty purposes.

If MMS cannot develop a value for royalty purposes using any of the valuation procedures previously mentioned, it could use a net-back procedure to value the gas by working backwards from the end use sales price to arrive at a value for royalty purposes at the lease. This last benchmark also would authorize MMS to use any other reasonable method to determine value.

The MMS particularly solicits comments regarding the valuation criteria and the prescribed order. Also, MMS is interested in receiving comments regarding any alternative methodologies for establishing value for royalty purposes in non-arm's-length or no contract situations which would be the least burdensome on both the lessee and MMS.

Proposed § 206.151(c) would provide that for all unprocessed gas disposed of other than pursuant to an

arm's-length contract covered by § 206.151(a), the lessee must propose to MMS what the reasonable value should be. The lessee would be required to supply any available data to support a proposal to treat a contract as an arm's-length equivalent pursuant to subsection (b)(2), or to support application of a particular criterion. MMS would use this data together with data it has available. The lessee's proposed valuation must be submitted to MMS within 30 days of the effective date of the final regulation for existing non-arm's length situations (and no contract situations), or within 30 days after it begins disposition of gas pursuant to a new arrangement. MMS would then issue a value determination. That determination would remain in effect for the period stated therein. At the end of the period, the lessee would be required to submit a new proposal.

So as not to cause unnecessary complications, proposed § 206.151(d), would permit the lessee to pay royalties at its proposed valuation until MMS issues its value determination. The lessee then would be entitled to a credit, or would be required to pay additional royalty, plus interest. If it was reasonable and in good faith, no penalties for improper reporting would be imposed for initially reporting the lower value, although penalties could be applied for other improper reporting.

Proposed § 206.151(e) would impose a diligent requirement on lessees. For example, if pursuant to an arm's-length contract a lessee could charge its purchaser a higher price as of a certain date, but the lessee fails to collect that additional money, it will be liable for royalty, plus interest, on the higher value. However, if the lessee enforces its right, but must do so through legal action, it is not required to pay the additional royalties until the legal proceedings are concluded.

Two of MMS' long-standing principles would be retained under § 206.151(f). First, under no circumstances

can the value for royalty purposes be less than the gross proceeds accruing, or which could accrue, to the lessee. Second, the gross proceeds accruing to the lessee includes all costs paid by the purchaser of the gas on behalf of the seller. This principle has been upheld in the following cases: *Wheless Drilling Co.*, 80 I.D. 599, 13 IBLA 21 (1973); *Amoco Production Co.*, 29 IBLA 234, 236 (1977); *Hoover & Bracken Energies, Inc.*, 52 IBLA 27, 88 ID 7 (1981), *aff'd*, 723 F. 2d 1388 (10th Cir. 1983). Thus, if the purchaser reimburses the seller or pays any costs on behalf of the seller, for such items as severance taxes, gathering, dehydration, measuring, or treating costs, then the seller must include those reimbursed costs as part of the gross proceeds upon which the royalty value is determined. The proposed rules retain the existing requirement that operations such as dehydration, compression, measurement, or field gathering are costs incurred to place the products in marketable condition and are to be borne exclusively by the lessee.

§ 206.151(g) of the proposed regulations would provide that where the royalty value is based on gross proceeds, that value would be increased to the extent those gross proceeds were reduced because the purchaser, or any other person, is providing certain services the cost of which ordinarily is the responsibility of the lessee to place the gas in marketable condition. By way of illustration, dehydration is a cost of making gas marketable which must be borne by the lessee. If the lessee enters into a contract where the purchaser agrees to dehydrate the gas and hence the contract price is reduced by 15 cents per Mcf, MMS would add the 15 cents per Mcf to the gross proceeds to determine the royalty value.

§ 206.151(h) of the proposed regulations would provide that the lessee is entitled to an allowance for the reasonable actual costs of transporting the royalty portion of gas to a sales point remote from the lease.

Proposed § 206.152, Valuation standards—processed gas, mirrors proposed § 206.151. The arm's-length philosophy and mechanism of establishing values for royalty purposes are the same, except values are established for all commodities resulting from processing gas, i.e., the principal product and the associated products. In view of this, a section-by-section analysis will not be repeated. However, it should be noted at this point that this proposed section would provide that the lessee is entitled to an allowance for the reasonable actual costs of processing the royalty portion of gas, as well as an allowance for the reasonable actual costs of transporting the royalty portion of principal products or associated products to a sales point remote from the plant.

Proposed § 206.153, Point of royalty settlement, subsection (a), would require that royalty be computed on the basis of the quantity and quality of unprocessed gas in marketable condition at the measurement location approved by MMS for offshore leases or by BLM for onshore leases. In those instances where the lessee sells unprocessed gas at conditions and/or locations other than those approved by BLM or MMS, the value of the unprocessed gas for royalty purposes must be determined under the conditions and at the location approved by BLM or MMS. Proposed § 206.153(b) would require that royalty be computed on the basis of the quantity and quality of the principal product and associated products produced by a processing plant and determined in accordance with 30 CFR 206.172.

Proposed § 206.154, Accounting for comparison, would provide that where a lessee, or a person to whom the lessee has transferred gas pursuant to a non-arm's-length contract or no contract situation, processes the lessees gas, the value for royalty purposes shall be the greater of 1) the value of the principal product and the associated products resulting from processing the gas, as adjusted for any approved processing or transportation deductions, or 2) the value of unprocessed gas.

Proposed § 207.150, Submittal requirements-contracts and sales agreements, subsection (a), states that all gas, principal products and associated products sales agreements and contracts, and changes and amendments thereto, and all other agreements or contracts affecting gross proceeds are to be submitted by the lessee for offshore and onshore Federal and Indian leases within 60 days of the effective date of the final rule or 60 days of execution, as appropriate. At the time of its contract submittals, the lessee would certify in writing that it has provided all documents and information which reflect the total consideration provided by the purchasers of gas, principal products and associated products from the lease. If the lessee falsely certifies, it would be subject to penalties and other sanctions pursuant to applicable laws and regulations. Subsection (b) would provide that all applicable posted price bulletins are to be submitted by the company issuing the bulletin with 30 days of initial distribution.

Subsection (c) would provide that lessees and other payors would be required to advise MMS whether the contract is arm's-length or non-arm's-length. A definition of arm's-length contract was included with the proposed coal valuation regulations. This designation is important since it would determine which valuation method would be used. It is not proposed to make this designation part of the certification.

The lessee's designation of a contract as arm's-length would not be conclusive. Subsection (c) would provide that MMS may audit those contracts to ascertain that the lessee's designation of a contract as arm's-length meets the criteria of MMS' arm's-length contract definition.

As an alternative, MMS is considering having lessees submit abstracts of contracts, etc., to reduce the volume of documents MMS must retain. Comments are specifically requested on this alternative.

III. Procedral Matters

Executive Order 12291

The DOI has determined that this document is not a major rule and does not require a regulatory analysis under Executive Order 12291. This proposed rulemaking is to consolidate Federal and Indian gas and associated products royalty valuation regulations; to clarify DOI gas and associated products royalty valuation policy; and to provide for consistent royalty valuation policy among all leasable minerals. This rulemaking is in response to recommendations by the Commission on Fiscal Accountability of the Nation's Energy Resources.

Lessee reporting requirements shall remain the same. All gas, principal products and associated products contracts, will be required to be submitted as under the existing regulations.

Regulatory Flexibility Act

Since this rule primarily consolidates and streamlines existing regulations for consistent application, there are no significant additional requirements or burdens placed upon small business entities as a result of implementation of this rule. Therefore, the DOI has determined that this rulemaking will not have a significant economic effect on a substantial number of small entities and does not require a regulatory flexibility analysis under the Regulatory Flexibility Act (5 U.S.C. 610 *et seq.*).

Paperwork Reduction Act

The information collection requirement located at § 207.150 of this rule has been approved by the Office of Management and Budget (OMB) under 44 U.S.C. 3504(h) and assigned OMB clearance numbers —— and ——.

National Environmental Policy Act of 1969

It is hereby determined that this rulemaking does not constitute a major Federal action significantly affecting

the human environment and a detailed statement pursuant to Section 102(2)(C) of the National Environmental Policy Act of 1969 (42 U.S.C. 4332(2)(C)) is not required.

Public Comment Procedures

A. Written Comments

You are invited to participate in this proceeding by submitting data, views or arguments with respect to this notice. All comments should be submitted by 4:30 p.m., d.s.t., of the day specified in the "DATES" section to the appropriate address indicated in the "ADDRESSES" section of this preamble and should be identified on the outside envelope and on documents submitted with the designation "Revision of Gas and Associated Products Royalty Valuation Regulations and Related Topics." Ten copies should be submitted. All comments received by the MMS will be available for public inspection in Room 2256, Building 41, Denver Federal Center, Lakewood, Colorado, between the hours of 8:00 a.m. and 4:00 p.m., Monday through Friday.

Any information or data submitted which you consider to be confidential must be so identified and submitted in writing, one copy only. MMS reserves the right to determine the confidential status of the information or data and to treat it according to its independent determination.

B. Public Hearing

1. Procedure for requests to make oral presentations: The time and place for the hearing are indicated in the "DATES" and "ADDRESSES" sections of the preamble. If necessary to present all testimony, the hearing will resume at 9:30 a.m. on the next business day following the first day of the hearing.

You may make a written request for an opportunity to make an oral presentation. The requests should contain a business telephone number and also a telephone number where you may be contacted during the day prior to the hearing. If you are selected to be heard at the hearing you will be notified before 4:30 p.m., ————, 1986. You will be required to submit 50 copies of your statement to MMS at the address indicated in the "ADDRESSES" section of the preamble by 4:30 p.m. ———, 1986.

2. Conduct of the hearing: MMS reserves the right to select the persons to be heard at the hearing (in the event there are more requests to be heard than time allows), to schedule their respective presentations, and to establish the procedures governing the conduct of the hearing. The length of each presentation may be limited, based upon the number of persons requesting to be heard.

A Department of the Interior official will be designated to preside at the hearing. This will not be a judicial-type hearing. Questions may be asked only by those conducting the hearing. At the conclusion of all initial oral statements, each person who has made an oral statement will be given the opportunity, if he or she so desires, to make a rebuttal statement. The rebuttal statement will be given in the order in which the initial statements were made and will be subject to time limitations.

If you wish to ask a question at the hearing, you may submit the question, in writing, to the presiding officer. The presiding officer will determine whether the question is relevant, and whether time limitations permit it to be presented for answer at the hearing.

Any further procedural rules needed for the proper conduct of the hearing will be announced by the presiding officer, at the opening of the hearing.

A transcript of the hearing will be made. The entire record of the hearing, including the transcript, will be

retained by the MMS and made available for inspection in Room 2256, Building 41, Denver Federal Center, Lakewood, Colorado, between the hours of 8:00 a.m. and 4:00 p.m., Monday through Friday. You may purchase a copy of the transcript from the reporter.

List of Subjects

30 CFR Part 202

Royalties, Minimum royalties, Gross proceeds, Reporting standards.

30 CFR Part 206

Royalties, Beneficial use, Posted price bulletins, Gas and associated products sales contracts, Reporting requirements, Benchmarks, Product valuation, Gross proceeds.

30 CFR Part 207

Oil, gas, principal products and associated products, Reporting requirements, Contracts, Sales agreements.

Under the authority of the Mineral Leasing Act of February 25, 1920, as amended (30 U.S.C. 181, *et seq.*); the Mineral Leasing Act for Acquired Lands of August 7, 1947, as amended (30 U.S.C. 351-359); the Tribal Leasing Act of 1938 (25 U.S.C. 396a, *et seq.*); the Allotted Indian Land Leasing Act of 1909 (25 U.S.C. 396); the OCS Lands Act of August 7, 1953, as amended (43 U.S.C. 1331); the Federal Oil and Gas Royalty Management Act of 1982 (30 U.S.C. 1701 et seq.); the Indian Mineral Development Act of 1982 (25 U.S.C. 2102); Chapter II, Title 30, Subchapter A, of the Code of Federal Regulations is amended as set forth below.

Date	Assistant Secretary for Land and Minerals Management

DEPARTMENT OF INTERIOR

Mineral Management Service

SUBCHAPTER A—ROYALTY MANAGEMENT

1. 30 CFR Chapter II; Subchapter A Parts 202 and 206 are amended by redesignating certain sections as shown in the following redesignation table.

Old Subchapter A Designation	New Subchapter A Designation
§ 206.105	§ 202.150
§ 206.106	§ 202.151
§ 206.107	Removed

2. 30 CFR Part 202 Subpart D is amended by adding new § 202.152 and by revising newly redesignated §§ 202.150 and 202.151 to read as follows:

PART 202—ROYALTIES

* * * *

Subpart D—Federal and Indian Gas and Associated Products

Sec.

202.150—Royalty on gas.

202.151—Royalty on processed gas.

202.152—Standards for reporting and paying royalties on gas, principal products and associated products.

* * * *

Subpart D—Federal and Indian Gas and Associated Products

§ 202.150 Royalty on Gas.

(a) The royalty on gas, except helium produced from Federal leases, shall be at the rate established by the terms of the lease. Royalty shall be paid in value unless the Department of the Interior requires payment in-kind.

(b) All gas (except gas unavoidably lost or used on, or for the benefit of, the lease) produced from a Federal or Indian lease subject to this part is subject to royalty. This includes gas used by the lessee off the lease.

§ 202.151 Royalty on processed gas.

(a) A royalty as provided in the lease for gas shall be paid on the value of the principal product and the associated products resulting from processing the gas produced from a lease subject to this part. MMS shall authorize a deduction from royalty payments for the reasonable actual costs of processing the royalty portion of gas produced from Federal and Indian leases. Processing allowances shall be determined in accordance with Subpart D of Part 206 of this Title.

(b) No royalty is due on the principal product and/or any associated product resulting from processing gas produced from a lease which is reinjected into a reservoir within the same lease, unit area, or communitized area, when the reinjection is included in a plan of development or operations and the plan has received BLM or MMS approval for onshore or offshore operations, respectively, until such time as they are finally produced from the reservoir for sale or use off-lease.

§ 202.152 Standards for reporting and paying royalties on gas, principal products and associated products.

(a) (1) Gas volumes and Btu content, if applicable, shall both be determined under the same degree of water saturation and shall be reported in units of one thousand cubic feet (Mcf) and at a rate of Btu's per cubic foot, respectively, at a standard pressure base of 14.73 pounds per square inch absolute (psia) and a standard temperature base of 60°F. Gas volumes and Btu content shall be reported for royalty purposes on the same water vapor

saturated or unsaturated basis prescribed by Federal Energy Regulatory Commission (FERC) regulation, or on the basis prescribed in the lessee's gas sales contract if the sales are not subject to FERC regulation, or the prescribed basis does not result in a conflict with FERC regulation.

(2) The frequency and method for Btu measurement as set forth in arm's-length contracts, and contracts treated as the equivalent of arm's-length contracts for royalty purposes in Part 206 of this Title, shall be used for reporting purposes. If the frequency and method of Btu measurement cannot be otherwise established, MMS will require that the Btu value be measured at least semiannually by recognized standard industry testing methods.

(b) Principal product and associated product volumes shall be reported as specified herein.

(1) Carbon dioxide (CO_2), nitrogen (N_2), helium (He) and hydrocarbon gas consisting principally of methane shall be reported in units of one thousand cubic feet (Mcf) at a standard pressure base of 14.73 pounds per square inch absolute (psia) and a standard temperature base of 60°F. These gas volumes and Btu content, if applicable, shall be reported for royalty purposes on the same water vapor saturated or unsaturated basis as described in paragraph (a) of this section.

(2) Natural gas liquids (NGL) volumes shall be reported in standard U.S. gallons (231 cubic inches) at 60°F.

(3) Sulphur volumes shall be reported in long tons (2240 pounds).

* * * *

3. 30 CFR Part 206 is amended by adding §§ 206.150, 206.151, 206.152, 206.153, and 206.154 to Subpart D to read as follows:

PART 206—PRODUCT VALUATION

* * * *

Subpart D—Federal and Indian Gas and Associated Products

Sec.

206.150—Purpose and scope.

206.151—Valuation standards—unprocessed gas.

206.152—Valuation standards—processed gas.

206.153—Point of royalty settlement.

206.154—Accounting for comparison.

* * * *

Subpart D—Federal and Indian Gas and Associated Products

§ 206.150 Purpose and Scope.

This subpart is applicable to Federal and Indian (tribal and allotted) oil and gas leases (except leases on the Osage Indian Reservation).

§ 206.151 Valuation standards—unprocessed gas.

(a) The value for royalty purposes of gas which is sold pursuant to an arm's-length contract prior to processing shall be the gross proceeds accruing, or which could accrue, to the lessee. If the sales point under the contract is different from the point of royalty settlement as it has been approved by BLM for onshore leases or MMS for offshore leases, the gross proceeds shall be increased, for royalty purposes, for the differences in quantity and quality of the gas between the two points. This paragraph does not apply where the lessee's arm's-length sales contract includes a provision reserving to the lessee the right to process the gas and the lessee exercises that right.

(b) (1) The value for royalty purposes of unprocessed gas produced from leases subject to this section and which is not sold pursuant to an arm's-length contract shall be the reasonable value determined by MMS in accordance with this section. This paragraph does not apply where the lessee, or a person to whom the lessee has transferred gas pursuant to a non-arm's-length contract or no contract situation, processes the lessee's gas.

(2) The reasonable value shall be the price received by the lessee under a non-arm's-length contract if MMS determines that the contract is similar to arm's-length contracts. The lessee must demonstrate, through the submittal of supporting documents, that its non-arm's-length contract is comparable in price, duration, terms, volume, time of execution, and other circumstances to arm's-length contracts for the sale of like-quality gas from the same field, (or if there is no arm's-length contract for the same field, then for a field in the area).

(3) If the reasonable value of unprocessed gas cannot be determined pursuant to subsections (a) or (b) (2), then the reasonable value shall be determined through application of other valuation criteria. MMS shall consider the criteria in the following order and shall determine the reasonable value based upon the first applicable criterion: (i) other prices being paid under representative, recently executed arm's-length contracts for similar-sized sales quanities of like-quality gas from the same field (or if there is no arm's-length contract for the same field, then for a field as near the lease as possible); (ii) all prices posted for gas, whether like-quality or not, from the same field (or if there is no posted price for gas from the same field, then a field as near the lease as possible); (iii) spot sales postings as near the lease as possible; (iv) prices reported for that gas to the Federal Energy Regulatory Commission (FERC) of the Department of Energy (DOE), or the Energy Information Administration (EIA) of the DOE; (v)

other relevant matters including information submitted by the lessee concerning circumstances unique to a particular lease operation or the saleability of certain types of gas; (iv) if MMS cannot determine a reasonable value for royalty purposes using subsections (i) through (v), it may use a net-back method or any other reasonable method to determine value; provided, however, that if the maximum price at which gas may be sold pursuant to the Natural Gas Policy Act of 1978, 15 U.S.C. 3301-3432, is less than the royalty value determined pursuant to this section, then MMS shall accept that maximum price as the royalty value.

(c) Where the value for royalty purposes is determined pursuant to subsection (b)(2) or (b)(3), the lessee shall propose to MMS what the reasonable value should be. The lessee shall submit all available data to support its proposal. The initial proposal must be submitted by [insert 30 days after effective date of final rule] or within 30 days after it begins the disposition of gas, whichever is later. MMS shall then determine the royalty value based upon the lessee's proposal and any additional information MMS deems necessary. That determination shall remain effective for the period stated therein, and at the end of that period, the lessee shall be required to propose a new value.

(d) Where the value for royalty purposes is determined pursuant to subsection (b)(2) or (b)(3), until MMS issues the value determination required by subsection (c), the lessee shall remit royalty payments based upon the value that the lessee has proposed for approval. When MMS determines the proper value for royalty purposes, the lessee shall be liable for the difference, if any, between royalty payments made based upon the proposed value and the royalty payments that are due based upon the value established by MMS. The lessee also shall be liable for interest computed pursuant to

30 CFR § 218.54, retroactive to the date of the value determination.

(e) Value for royalty purposes shall be based on the highest price a prudent operator may receive under its contract. If the lessee fails to take proper or timely action to receive price increases to which it is entitled, it must pay royalty at a value based upon that obtainable price. If the lessee makes timely application for a price increase allowed under its contract but the purchaser refuses, and the lessee takes legal action to force purchaser compliance, the lessee will owe no additional royalties until monies or consideration resulting from the price increase are received.

(f) Under no circumstances shall the value for royalty purposes be less than the gross proceeds accruing, or which could accrue, to the lessee. For purposes of this section, gross proceeds includes, but is not limited to, reimbursement for dehydration, compression, measurement, or field gathering to the extent that the lessee is obligated to perform it at no cost to the lessor; reimbursements, payments or credits for advanced prepaid reserve payments subject to recoupment through reduced prices in later sales; exploration or development costs that are subject to recoupment through reduced prices in later sales; take-or-pay payments; reimbursements for transportation; tax reimbursements; and other reimbursements.

(g) Where the royalty value established pursuant to this section is determined by a lessee's gross proceeds, that value shall be increased to the extent that the gross proceeds have been reduced because the purchaser, or any other person, is providing certain services, the cost of which ordinarily is the responsibility of the lessee, to place the product in marketable condition.

(h) The lessee shall be entitled to an allowance for the reasonable actual costs of transporting the royalty

portion of gas to a sales point remote from the lease. Transportation allowances shall be determined in accordance with § 206.30 of this part.

(i) The method and amount of an approved valuation is not proprietary information and shall be made publicly available. The data from which a valuation is derived, however, is considered to be proprietary in nature and will be maintained in a confidential manner in accordance with applicable laws and regulations.

§ 206.152 Valuation standards—processed gas.

(a) Where gas is processed prior to its sale, the value for royalty purposes shall be the value of the principal product and associated products resulting from processing the gas as determined pursuant to this section. This section applies to arm's-length contracts for the sale of gas prior to processing where that contract includes a provision reserving to the lessee the right to process the gas and the lessee exercises that right, and those situations where a person to whom the lessee has transferred gas pursuant to a non-arm's-length contract or no contract situation processes the lessee's gas.

(b) The value for royalty purposes of principal products or associated products which are sold pursuant to an arm's-length contract shall be the gross proceeds accruing, or which could accrue, to the lessee. The gross proceeds shall be increased, for royalty purposes, when such proceeds are based on quantities of principal products and/or associated products that are less than those quantities required by § 206.172 of this subpart.

(c) (1) The value for royalty purposes of principal products or associated products from leases subject to this section and which are not sold pursuant to an arm's-length contract shall be the reasonable value determined by MMS in accordance with this section.

(2) The reasonable value shall be the price received by the lessee under a non-arm's-length contract if MMS

determines that the contract is similar to arm's-length contracts. The lessee must demonstrate, through the submittal of supporting documents, that its non-arm's-length contract is comparable in price, duration, terms, volume, time of execution, and other circumstances to arm's-length contracts for the sale of like-quality products from the same field or plant (or if there is no arm's-length contract for the same field or plant, then for a field or plant in the area).

(3) If the reasonable value of principal products or associated products cannot be determined pursuant to subsections (b) or (c)(2), then the reasonable value shall be determined through application of other valuation criteria. MMS shall consider the criteria in the following order and shall determine the reasonable value based upon the first applicable criterion: (i) other prices being paid under representative, recently executed arm's-length contracts for similar-sized sales quantities of like-quality products from the same field or plant (or if there is no arm's-length contract for the same field or plant, then for a field or plant as near the lease as possible); (ii) all prices posted for that product, whether like-quality or not, from the same field or plant (or if there is no posted price for that product from the same field or plant, then a field or plant as near the lease as possible); (iii) spot sales postings as near the lease or plant as possible; (iv) prices reported for that product to the Federal Energy Regulatory Commission (FERC) of the Department of Energy (DOE), or the Energy Information Administration (EIA) of the DOE; (v) other relevant matters including information submitted by the lessee concerning circumstances unique to a particular lease or plant operation or the saleability of certain types of products; (iv) if MMS cannot determine a reasonable value for royalty purposes using subsections (i) through (v), it may use a net-back method or any other reasonable method to determine value; provided, however, that if the maximum

price at which gas may be sold pursuant to the Natural Gas Policy Act of 1978, 15 U.S.C. 3301-3432, is less than the royalty value determined pursuant to this section, then MMS shall accept that maximum price as the royalty value.

(d) Where the value for royalty purposes is determined pursuant to subsection (c)(2) or (c)(3), the lessee shall propose to MMS what the reasonable value should be. The lessee shall submit all available data to support its proposal. The initial proposal must be submitted by [insert 30 days after effective date of final rule] or within 30 days after the initiation of processing, whichever is later. MMS shall then determine the royalty value based upon the lessee's proposal and any additional information MMS deems necessary. That determination shall remain effective for the period stated therein, and at the end of that period, the lessee shall be required to propose a new value.

(e) Where the value for royalty purposes is determined pursuant to subsection (c)(2) or (c)(3), until MMS issues the value determination required by subsection (d), the lessee shall remit royalty payments based upon the value that the lessee has proposed for approval. When MMS determines the proper value for royalty purposes, the lessee shall be liable for the difference, if any, between royalty payments made based upon the proposed value and the royalty payments that are due based upon the value established by MMS. The lessee also shall be liable for interest computed pursuant to 30 CFR § 218.54, retroactive to the date of the value determination.

(f) Value for royalty purposes shall be based on the highest price a prudent operator may receive under its contract. If the lessee fails to take proper or timely action to receive price increases to which it is entitled, it must pay royalty at a value based upon that obtainable price. If the lessee makes timely application for a price

increase allowed under its contract but the purchaser refuses, and the lessee takes legal action to force purchaser compliance, the lessee will owe no additional royalties until monies or consideration resulting from the price increase are received.

(g) Under no circumstances shall the value for royalty purposes be less than the gross proceeds accruing, or which could accrue, to the lessee. For purposes of this section, gross proceeds includes, but is not limited to, reimbursement for dehydration, compression, measurement, or field gathering to the extent that lessee is obligated to perform it at no cost to the lessor; reimbursements, payments or credits for advanced prepaid reserve payments subject to recoupment through reduced prices in later sales; exploration or development costs that are subject to recoupment through reduced prices in later sales; take-or-pay payments; reimbursements for transportation; tax reimbursements; and other reimbursements.

(h) Where the royalty value established pursuant to this section is determined by a lessee's gross proceeds, that value shall be increased to the extent that the gross proceeds have been reduced because the purchaser, or any other person, is providing certain services, the cost of which ordinarily is the responsibility of the lessee, to place the product in marketable condition.

(i) The lessee shall be entitled to an allowance for the reasonable actual costs of processing the royalty portion of gas. Processing allowances shall be determined in accordance with § 206.170 through § 206.174 of this subpart.

(j) When the sales point for principal products or associated products is remote from the plant, the lessee shall be entitled to an allowance for the reasonable actual cost of transporting the royalty portion of principal products or associated products to that sales point. Trans-

portation allowances shall be determined in accordance with § 206.30 of this Part.

(k) The method and amount of an approved valuation is not proprietary information and shall be made publicly available. The data from which a valuation is derived, however, is considered to be proprietary in nature and will be maintained in a confidential manner in accordance with applicable laws and regulations.

§ 206.153 Point of royalty settlement.

(a) Royalties shall be complied, as a minimum, on the basis of the quantity and quality of unprocessed gas in marketable condition at the point approved by BLM or MMS for onshore and offshore leases, respectively.

(b) Royalties shall be computed on the basis of the quantity and quality of the principal product and the associated products produced by a processing plant. The quantities of the principal product and the associated products for royalty purposes shall be determined in accordance with § 206.172 of this subpart.

§ 206.154 Accounting for comparison.

Where the lessee, or a person to whom the lessee has transferred gas pursuant to a non-arm's-length contract or no contract situation, processes the lessee's gas, the value for royalty purposes shall be the greater of (1) the value of the principal product and the associated products resulting from processing the gas (as adjusted for any approved processing and/or transportation deductions), or (2) the value of the unprocessed gas, as determined pursuant to this part.

* * * *

4. 30 CFR Part 207 is amended by adding § 207.150 to Subpart D to read as follows:

PART 207—SALES AGREEMENTS OR CONTRACTS GOVERNING THE DISPOSAL OF OIL AND GAS LEASE PRODUCTS

* * * *

Subpart D—Federal and Indian Gas and Associated Products

Sec.

207.150 Submittal requirements—contracts and sales agreements.

* * * *

Subpart D—Federal and Indian Gas and Associated Products

§ 207.150 Submittal requirements—contracts and sales agreements.

(a) Lessees shall submit to the MMS all active contracts governing the disposition of gas, principal products and associated products from Federal and Indian leases, and changes and amendments thereto, which are executed on or before [insert effective date of final rule]. Contracts must be received by MMS by [insert 60 days after effective date of final rule]. Contracts and contractual amendments for the sale of gas, principal products and associated products from Federal and Indian leases which are executed after [insert effective date of final rule] must be received by MMS within 60 days of the date of execution. Lessees shall include as part of the submittal requirements any contracts, agreements or other documents which affect the gross proceeds received for the sale of gas, principal products and associated products as well as any other information regarding any consideration received for the sale or disposition of gas, principal products and associated products which is not included in such contracts. At the time of its contract submittals, the lessee shall certify in writing that it has provided all documents and information which reflect the total consid-

eration provided by purchasers for gas, principal products and associated products from leases subject to this subpart. Contracts, contract amendments, certifications, and other information shall be sent to MMS at the following address:

Minerals Management Service
Royalty Valuation and Standards Division
Denver, Colorado 80225

(b) All posted price bulletins applicable to gas, principal products and associated products produced from Federal, onshore and offshore, and Indian leases, and changes and amendments thereto, are to be submitted to MMS by the person issuing the bulletin within 30 days of initial distribution.

(c) Lessees shall designate for each contract submitted pursuant to this section whether the contract either is arm's-length or non-arm's-length. A lessee's determination that its contracts are arm's-length is subject to future audit to verify that the contract meets the criteria of the arm's-length contract definition in § 206.5 of this Part.

* * * *

5. Notice to Lessees and Operators of Federal and Indian Onshore Oil and Gas Leases (NTL-5) is rescinded.

6. (NTL-1)

7. (NTL-1A)

APPENDIX L

EXHIBIT "A"

LEASE NO. .....

CONTRACT NO. .....

UNITED STATES
DEPARTMENT OF THE INTERIOR
BUREAU OF INDIAN AFFAIRS

OIL AND GAS MINING LEASE—
TRIBAL INDIAN LANDS

THIS INDENTURE OF LEASE, made and entered into in quintuplicate this .... day of ....., 19...., by and between .....

.....

.....

of ....., State of ....., for and on behalf of the ..... Tribe of Indians, lessor, and .....

.....

.....

of ....., State of ....., lessee, WITNESSETH:

1. Lessor, in consideration of a cash bonus of $....., paid to the payee designated by the Area Director, receipt of which is hereby acknowledged and in consideration of rents and royalties to be paid, and the covenants to be observed as herein set forth, does hereby grant and lease to the lessee the exclusive right and privilege to drill for, mine, extract, remove, and dispose of all

the oil and natural gas deposits including helium gas, carbon dioxide gas, and sulphur gas in or under the following-described tracts of land situated in the county of ....., State of ....., and more particularly described as follows:

containing ..... acres more or less, together with the right to construct and maintain thereupon all works, buildings, plants, waterways, roads, telegraph and telephone lines, pipe lines, reservoirs, tanks, pumping stations, or other structures necessary to the full enjoyment hereof for the term of 10 years from and after the approval hereof by the Secretary of the Interior and as much longer thereafter as oil and/or gas is produced in paying quantities from said land.

2. The term "oil and gas supervisor" as employed herein shall refer to such office or officers as the Secretary of the Interior may designate to supervise oil and gas operations on Indian lands. The term "superintendent" as used herein shall refer to the superintendent or other official in charge of the Indian Agency having jurisdiction over the lands leased. Helium gas, carbon dioxide gas, sulphur gas, and all other natural gases are included under the "gas" as used in this lease.

3. In consideration of the foregoing, the lessee hereby agrees:

(*a*) Bond.—To furnish such bond as may be required by the regulations of the Secretary of the Interior, with satisfactory surety, or United States bonds as surety therefor, conditioned upon compliance with the terms of this lease.

(*b*) Wells.—(1) To drill and produce all wells necessary to offset or protect the leased land from drainage or in lieu thereof, to compensate the lessor in full each month for the estimated loss of royalty through drainage: *Provided*, That during the period of supervision by the Secretary of the Interior, the necessity for offset wells shall be determined by the oil and gas supervisor and

payment in lieu of drilling and production shall be with the consent of, and in an amount determined by the Secretary of the Interior; (2) at the election of the lessee to drill and produce other wells: *Provided*, That the right to drill and produce such other wells shall be subject to any system of well spacing or production allotments authorized and approved under applicable law or regulations, approved by the Secretary of the Interior and affecting the field or area in which the leased lands are situated; and (3) if the lessee elects not to drill and produce such other wells for any period the Secretary of the Interior may, within 10 days after due notice in writing, either require the drilling and production of such wells to the number necessary, in his opinion, to insure reasonable diligence in the development and operation of the property, or may in lieu of such additional diligent drilling and production require the payment on and after the first anniversary date of this lease of not to exceed $1 per acre per annum, which sum shall be in addition to any rental or royalty hereinafter specified.

(*c*) Rental and royalty.—To pay, beginning with the date of approval of the lease by the Secretary of the Interior or his duly authorized representative, a rental of $1.25 per acre per annum in advance during the continuance hereof, the rental so paid for any one year to be credited on the royalty for that year, together with a royalty of 16⅔ percent of the value or amount of all oil, gas, and/or natural gasoline, and/or all other hydrocarbon substances produced and saved from the land leased herein, save and except oil, and/or gas used by the lessee for development and operation purposes on said lease, which oil or gas shall be royalty free. During the period of supervision, "value" for the purposes hereof may, in the discretion of the Secretary, be calculated on the basis of the highest price paid or offered (whether calculated on the basis of short or actual volume) at the time of production for the major portion of the oil of the same

gravity, and gas, and/or natural gasoline, and/or all other hydrocarbon substances produced and sold from the field where the leased lands are situated, and the actual volume of the marketable product less the content of foreign substances as determined by the oil and gas supervisor. The actual amount realized by the lessee from the sale of said products may, in the discretion of the Secretary, be deemed mere evidence of or conclusive evidence of such value. When paid in value, such royalties shall be due and payable monthly on the last day of the calendar month following the calendar month in which produced; when royalty on oil produced is paid in kind, such royalty oil shall be delivered in tanks provided by the lessee on the premises where produced without cost to the lessor unless otherwise agreed to by the parties thereto, at such time as may be required by the lessor: *Provided,* That the lessee shall not be required to hold such royalty oil in storage longer than 30 days after the end of the calendar month in which said oil is produced: *And provided further,* That the lessee shall be in no manner responsible or held liable for loss or destruction of such oil in storage caused by the acts of God. All rental and royalty payments, except as provided in section 4 (*c*) shall be made by check or draft drawn on a solvent bank, open for the transaction of business on the day the check or draft is issued, to the payee designated by the Area Director. All such rental and royalty payments shall be mailed to the oil and gas supervisor for transmittal to the payee designated by the Area Director. It is understood that in determining the value for royalty purposes of products, such as natural gasoline, that are derived from treatment of gas, a reasonable allowance for the cost of manufacture shall be made, such allowance to be two-thirds of the value of the marketable product unless otherwise determined by the Secretary of the Interior on application of the lessee or on his own initiative, and that royalty will be computed on the value of gas or casinghead gas, or on the products thereof (such as residue

gas, natural gasoline, propane, butane, etc.), whichever is the greater.

(*d*) Monthly statements.—To furnish to the oil and gas supervisor monthly statements in detail in such form as may be prescribed by the Secretary of the Interior, showing the amount, quality, and value of all oil, gas, natural gasoline, or other hydrocarbon substances produced and saved during the preceding calendar month as a basis upon which to compute, for the treasurer of said tribe or the superintendent, the royalty due the lessor. The leased premises and all wells, producing operations, improvements, machinery, and fixtures thereon and connected therewith and all books and accounts of the lessee shall be open at all times for the inspection of any duly authorized representative of the Secretary of the Interior.

(*e*) Log of well.—To keep a log in the form prescribed by the Secretary of the Interior of all the wells drilled by the lessee showing the strata and character of the formations passed through by the drill, which log or a copy thereof shall be furnished to the oil and gas supervisor.

(*f*) Diligence, prevention of waste.—To exercise reasonable diligence in drilling and operating wells for oil and gas on the lands covered hereby, while such products can be secured in paying quantities; to carry on all operations hereunder in a good and workmanlike manner in accordance with approved methods and practice, having due regard for the prevention of waste of oil or gas developed on the land, or the entrance of water through wells drilled by the lessee to the productive sands or oil or gas-bearing strata to the destruction or injury of the oil or gas deposits, the preservation and conservation of the property for future productive operations, and to the health and safety of workmen and employees; to plug securely all wells before abandoning the same and to effectually shut off all water from the oil or gas-bearing strata; not to drill any well within 200 feet of any house

or barn now on the premises without the lessor's written consent; to carry out at the expense of the lessee all reasonable orders and requirements of the oil and gas supervisor relative to prevention of waste, and preservation of the property and the health and safety of workmen; to bury all pipe lines crossing tillable lands below plow depth unless other arrangements therefor are made with the superintendent; to pay the lessor all damages to crops, buildings, and other improvements of the lesser occasioned by the lessee's operations: *Provided*, That the lessee shall not be held responsible for delays or casualties occasioned by causes beyond the lessee's control.

(*g*) Regulations.—To abide by and conform to any and all regulations of the Secretary of the Interior now or hereafter in force relative to such leases, including 30 CFR 221: *Prodvided*, That no regulation hereafter approved shall effect a change in rate of royalty or annual rental herein specified without the written consent of the parties to this lease.

(*h*) Assignment of lease.—Not to assign this lease or any interest therein by an operating agreement or otherwise nor to sublet any portion of the leased premises before restrictions are removed, except with the approval of the Secretary of the Interior. If this lease is divided by the assignment of an entire interest in any part of it, each part shall be considered a separate lease under all the terms and conditions of the original lease.

4. The lessor expressly reserves:

(*a*) Disposition of surface.—The right to lease, sell, or otherwise dispose of the surface of the lands embraced within this lease under existing law or laws hereafter enacted, such disposition to be subject at all times to the right of the lessee herein to the use of so much of said surface as is necessary in the extraction and removal of oil and gas from the land herein described.

(*b*) Use of gas.—The right to use sufficient gas free of charge for any school or other buildings belonging to the tribe on said lands by making connection at its own expense with the well or wells thereon, the use of such gas to be at the lessor's risk at all times.

(*c*) Royalty in kind.—The right to elect on 30 days' written notice to take lessor's royalty in kind.

5. Surrender and termination.—The lessee shall have the right at any time during the term hereof to surrender and terminate this lease or any part thereof upon the payment of the sum of one dollar and all rentals, royalties, and other obligations due and payable to the lessor; and in the event restrictions have not been removed, upon a showing satisfactory to the Secretary of the Interior that full provision has been made for conservation and protection of the property and the proper abandonment of all wells drilled on the portion of the lease surrendered, the lease to continue in full force and effect as to the lands not so surrendered. If this lease has been recorded lessee shall file a recorded release with his application to the superintendent for termination of this lease.

6. Cancelation and forfeiture.—When, in the opinion of the Secretary of the Interior and the Tribal Counsel, there has been a violation of any of the terms and conditions of this lease, the Secretary of the Interior shall have the right at any time after 30 days' notice to the lessee, specifying the terms and conditions violated, and after a hearing, if the lessee shall so request within 30 days of receipt of notice, to declare this lease null and void, and the lessor shall then be entitled and authorized to take immediate possession of the land: *Provided,* That after restrictions are removed the lessor shall have and be entitled to any available remedy in law or equity for breach of this contract by the lessee.

7. Removal of buildings, improvements, and equipment.—Lessee shall be the owner of and shall have the right to

remove from the leased premises, within 90 days after termination of this lease, any and all buildings, structures, casing, material, and/or equipment placed thereon for the purpose of development and operation hereunder, save and except casing in wells and other material, equipment, and structures necessary for the continued operation of wells producing or capable of being produced in paying quantities as determined by the Secretary of the Interior, on said leased land at the time of surrender of this lease or termination thereof; and except as otherwise provided herein, all casing in wells, material, structures, and equipment shall be and become the property of the lessor.

8. Drilling and producing restrictions.—It is covenanted and agreed that the Secretary of the Interior may impose restrictions as to time or times for the drilling of wells and as to the production from any well or wells drilled when in his judgment such action may be necessary or proper for the protection of the natural resources of the leased land and the interests of the Indian lessor, and in the exercise of his judgment the Secretary may take into consideration, among other things, Federal laws, State laws, or regulations by competent Federal or State authorities or lawful agreements among operators regulating either drilling or production, or both.

9. Unit operation.—The parties hereto agree to subscribe to and abide by any agreement for the cooperative or unit development of the field or area, affecting the leased lands, or any pool thereof, if and when collectively adopted by a majority operating interest therein and approved by the Secretary of the Interior, during the period of supervision.

10. Conservation.—The lessee in consideration of the rights herein granted agrees to abide by the provisions of any act of Congress, or any order or regulation prescribed pursuant thereto, relating to the conservation, pro-

duction, or marketing of oil, gas, or other hydrocarbon substances.

11. Heirs and successors in interest.—It is further covenanted and agreed that each obligation hereunder shall extend to and be binding upon, and every benefit hereof shall inure to, the heirs, executors, administrators, successors of, or assigns of the respective parties hereto.

12. No lease, assignment thereof, or interest therein, will be approved to any employee or employees of the United States Government whether connected with the Indian Service or otherwise and no employee of the Interior Department shall be permitted to acquire any interest in any mineral lease covering restricted Indian lands by ownership of stock in corporations having such leases or in any other manner.

IN WITNESS WHEREOF, the said parties have hereunto subscribed their names and affixed their seals on the day and year first above mentioned:

Two witnesses to execution by lessor:

_____ [SEAL]

_____

P. O. _____

_____ _____ [SEAL]

P. O. _____

To witnesses to execution by lessee:

_____ [SEAL]

_____

P. O. _____

_____

P. O. _____ Attest: _____

ACKNOWLEDGMENT OF LESSOR

STATE OF)
) ss:
COUNTY OF)

Before me, a notary public, on this —— day of ——— 19—, personally appeared _____ to me known to be the identical person who executed the within and foregoing lease, and acknowledged to me that ——— executed the same as ——— free and voluntary act and deed for the uses and purposes therein set forth.

_____

My commission expires ——

DEPARTMENT OF THE INTERIOR

BUREAU OF INDIAN AFFAIRS

———————, 19—

APPROVED: _____

Area Director.

9-361
(Rev. Apr. 1962)

Form approved.
Budget Bureau No. 42-R361.5.

UNITED STATES
DEPARTMENT OF THE INTERIOR
GEOLOGICAL SURVEY

Land Office .....

Lease No. .....

LESSEE'S MONTHLY REPORT OF SALES AND ROYALTY

Lessee ..... Month ....., 196....

Location ..... (Section) (T.) (R.) (M.)

Field ..... County ..... State .....

Following are ALL runs and sales made this month

(If no runs or sales of any products were made, state NONE under the appropriate heading)

OIL

Tank No.	Date	Net Barrels Run	Gravity	Price Per Barrel	Value
		Total Barrels Run	Average Price		Total Value

Purchaser of Above Oil

GAS

Sales in 1,000 Cu. Ft. @ 10 oz. and 14.4*	Price per 1,000 Cu. Ft.	Value
Total	Average	Total

Purchaser of Above Gas

GASOLINE

Sales in Gallons	Price Per Gallon	Value
Total	Average	Total

Purchaser of Above Gasoline

BUTANE AND OTHER LIQUID PRODUCTS

Sales in Gallons	Price Per Gallon	Value
Total	Average	Total

Purchaser of Above Butane or Other Liquid Products

Number of Oil Producing Wells Affecting Royalty Computations .....

ROYALTY

Product	Sales	Royalty Rate	Royalty Quantity	Royalty Value
OIL (Barrels)			*	
GAS (1,000 Cu. Ft.)			*	
GASOLINE (Gallons)			*	
BUTANE and Other Liquid Prod.			*	
Total Value of Royalty				

*Where applicable state "None"

ACKNOWLEDGMENT

I have read and examined the statements made hereon and find them true, accurate, and complete.

(*Signature and title of officer authorized to sign for lessee*)

..... (Lessee or Operator)

The United States Criminal Code, 18 U. S. C. 1001, makes it a criminal offense to make a willfully false statement or representation to any Department or Agency of the United States as to any matter within its jurisdiction.

This form to be properly prepared and filed IN DUPLICATE with the supervisor. Sales may be itemized on any other convenient form and attached to this report.

U.S. GOVERNMENT PRINTING OFFICE 1964—O-755-650

BEST AVAILABLE COPY

3878

Supreme Court, U.S.
FILED
SEP 17 1986
JOSEPH F. SPANIOL, JR.
CLERK

Nos. 86-225
86-219
86-224
86-226

IN THE

Supreme Court of the United States

OCTOBER TERM, 1986

SOUTHERN UNION COMPANY,
UNICON PRODUCING COMPANY,
SOUTHLAND ROYALTY COMPANY, and
EXXON CORPORATION,

Petitioners,

v.

JICARILLA APACHE TRIBE,
DONALD P. HODEL, Secretary of the
United States Department of the Interior,
and STATE OF NEW MEXICO,

Respondents.

On Petition For a Writ of Certiorari To The United States Court of Appeals For The Tenth Circuit

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BRIEF IN OPPOSITION OF RESPONDENT JICARILLA APACHE TRIBE

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QUESTIONS PRESENTED

Petitioners have presented eleven different questions in four separate Petitions for a Writ of Certiorari. Respondents submit, however, that the real issues are the following:

1. Whether the Secretary made an earlier administrative determination of value or had in fact merely accepted the Petitioners' royalty payments without review or audit.

2. Whether the Secretary's determination that dual accounting was required was reasonable and in accordance with the Secretary's fiduciary obligation.

3. Whether the Secretary's interpretation of the regulations and his requirement of an accounting by the Petitioners involves an important question of federal law warranting consideration by this Court.

LIST OF PARTIES

In order to clarify the relationship of the parties at the times pertinent to this case, Respondent sets forth the following relationships of the parties that have existed during the periods the leases were entered into and amended and during the periods the gas purchase contracts in suit were executed by the parties.

The predecessor of Southern Union Company was Southern Union Gas Company. Gas Company of New Mexico was the operating division in New Mexico of Southern Union Gas Company. As set forth in note 2 on page 6 of Southern Union Company's (SUG) brief, Southern Union sold substantially all of the assets of Gas Company of New Mexico (GCNM) to Public Service Company of New Mexico (PNM). SUG claims that as part of that sale, SUG retained certain liabilities including liability up to date of sale for additional royalties which may be assessed in this litigation. SUG does not state what the disposition would be of royalties held by the District Court in escrow or additional royalties paid to the Tribe since judgment and reimbursed to the producing companies by SUG. Counsel for SUG has advised counsel for Respondent that the Public Service Commission of New Mexico would determine what the disposition would be of any proceeds heretofore paid by the tribe and reimbursed by SUG to the other producing Petitioners under contracts for reimbursement with SUG, in the event the District Court decision is reversed.

Southern Union Production Company (SUPC), predecessor of Supron Energy Corporation (Supron), now

Unicon Producing Company, was a wholly owned subsidiary of Southern Union Gas Company when the leases from the Jicarilla Apache Tribe (the Tribe) were issued to SUG, and the gas purchase contracts at issue herein were executed by SUG and SUPC.

The predecessor of Southland Royalty Company (Southland), Aztec Oil and Gas Company (Aztec), was a wholly owned subsidiary of SUG when the leases from the Tribe were issued to SUG and the gas purchase contracts at issue herein were executed by SUG and Aztec.

The importance of the relationships of these parties to the issues in this case is set forth below in this brief.

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BRIEF IN OPPOSITION OF RESPONDENT JICARILLA APACHE TRIBE

This brief is filed in response to briefs of Southern Union Company, Unicon Producing Company, Southland Royalty Company, Exxon Company and amici Conoco, Inc. and Tenneco Oil Company.

OPINIONS BELOW

Respondent adopts the statement of Opinions Below shown on pages 1 to 3 of the Petition of Southern Union Company. Respondent adds to the statements of the Petitioners with respect to the Opinions Below in Respondent's Statement of the Case.

JURISDICTION

The Statement of Jurisdiction contained in the brief of Petitioner Southern Union Company, pages 3 through 4, is adopted by Respondent.

STATUTES AND REGULATIONS INVOLVED

The statement of Petitioner Southern Union Company as to Statutes and Regulations Involved shown on page 4 of said Petition is adopted by Respondent.

STATEMENT OF THE CASE

Petitioners' Joint Appendix will be designated Pet. Jt. App. Respondent's Appendix filed herein will be designated Resp. App.

The Statement of the Case contained in various petitioners' briefs is supplemented and corrected as follows:

The Jicarilla Apache Tribe (hereinafter called "the Tribe") brought this action in the United States District Court for the District of New Mexico on May 7, 1975 against Southern Union Gas Company (SUG) (subsequently Gas Company of New Mexico, (GCNM)), Southern Union Production Company (SUPC) (later Supron Energy Corporation, (Supron)), Aztec Oil and Gas Company (later Southland Royalty Company (Southland)), Exxon Company, U.S.A. (Exxon), and Southern Union Gathering Company (SUGC).

On November 10, 1976, the Tribe settled with GCNM and SUGC pursuant to a Stipulation of Settlement approved by the Court dismissing the Tribe's claims with prejudice against those two Defendants on payment of $600,000 cash to the Tribe and other considerations.

In December, 1976, the USGS Oil and Gas Supervisor ordered lessees to pay royalties for 1971, 1972 and 1973 based on certain minimum prices. In response, Southland paid $16,751.86 and Supron paid $247,374.18. Supron also paid additional royalties of $146,842.24 on liquids in the gas stream for 1974, 1975 and 1976.

The Tribe claimed damages from the corporate Defendants in the amount of the difference between royalties paid from January 1970 and royalties based on market value of gas and liquid hydrocarbons extracted from gas, and that said damages be trebled in accordance with the provisions of the federal antitrust laws, or in the alternative, cancellation of the leases. Against the Secretary of the Interior (the Secretary), the Tribe sought an order that the Secretary had breached his fiduciary obligations to the Tribe and requested a direction that the Secretary carry

out his fiduciary obligations in the area of accounting for oil, gas and liquid hydrocarbon substances, that he require dual accounting, require development of leases, and require offset wells; or in the alternative that the Court take the action requested on behalf of the Secretary for action unlawfully taken or unreasonable delayed.

The case went to trial in May and June of 1979 before the Court without a jury. The Court entered an Order on November 5, 1979 (Pet. Jt. App. 104a) holding with respect to the Tribe's anti-trust claims that although the Tribe had proved technical violations of the Clayton Act by maintaining interlocking directorates that the corporate defendants did not monopolize the market for liquid hydrocarbon substances and generally held against the Tribe on the anti-trust claims. The Court did not address directly plaintiff's claims that the defendant monopolized the *intrastate* markets for natural gas in New Mexico. The Court found that the Secretary failed to require dual accounting for liquid hydrocarbon substances in computing and paying royalties for production from lands on the reservation and ordered the Secretary to submit an accounting setting forth the additional amounts, if any, that the Secretary determined were due and owing to the Tribe, pursuant to dual accounting methods and determinations of value for natural gas. Following various accountings and reaccountings to the court, on July 30, 1980 (Pet. Jt. App. 141a), the Court ordered that, in addition to the dual accounting requirement, the Secretary of the Interior could also consider a minimum value based upon price received by Defendants in computing royalties owed by the Defendants. The Court held that "value"

for royalty purposes could exceed the prices set forth by the Natural Gas Policy Act of 1978, 15 U.S.C. §§ 3301-3432, and by the New Mexico Natural Gas Pricing Act, N.M. Stat. Ann. §§ 62-7-1, *et seq.*, (1978 & Supp. 1979), and made certain findings concerning calculations of the manufacturing allowance used in dual accounting and concerning accounting for royalties on gas lost between the wellhead and the inlet of the liquids manufacturing plant. (Pet. Jt. App. 141a-153a.)

On June 1, 1981 the Court pursuant to its Memorandum Opinion and Order of that date, awarded judgment in favor of the Tribe and against the lessee Defendants in the amounts set forth in the Secretary's accounting as approved and awarded various crossclaim judgments against Gas Company of New Mexico as follows: (Pet. Jt. App. 165a-174a).

The Tribe was awarded $24,144.50 from Southland;
The Tribe was awarded $262,087.24 from Supron;
The Tribe was awarded $57,705.07 from Exxon;
Southland was awarded $97,352.67from GCNM;
Supron was awarded $232,528.23 from GCNM;
Exxon was awarded $28,817.94 from GCNM;

The Court denied a Motion to Intervene by the State of New Mexico. The various defendants filed appeals from the Final Judgment of the Court. The Tribe filed a Notice of Appeals and Cross-Appeals on August 7, 1981.

A panel of three judges of the Tenth Circuit Court of Appeals reversed the decision of Judge Mechem as to the issues concerning dual acounting, applicability of the New Mexico Gas Pricing Act (NMGPA) to the valuation of royalties payable to the Tribe and breach of fiduciary duty of the Secretary, and affirmed the judgment of the District Court as to the antitrust issues. *Jicarilla Apache Tribe v.*

Supron Energy Corp. et al., 728 F.2d 1555 (10th Cir. 1984). (Pet. Jt. App. 21a-57a).

The Tribe filed a Motion for Rehearing and Suggestion of Rehearing En Banc on March 8, 1984. The Motion for Rehearing was granted by the Court on March 30, 1984.

On rehearing the Court of Appeals issued an *en banc* opinion on January 23, 1986 adopting the dissenting opinion of Judge Seymour. *See* the February 23, 1984 opinion of the Court of Appeals. 728 F.2d 1563 (Pet. Jt. App. 1a-14a). On June 18, 1986 the Court supplemented its *en banc* opinion, disagreeing with the Defendants' argument that the government should pay additional royalties owing to the Tribe as a result of this case because their non-payment resulted from the government's breach of fiduciary duty, distinguishing *Nevada v. United States,* 463 U.S. 110, 114, n. 16 (1983). The Court stated that the failure of the Secretary to require dual accounting resulted in the lessees paying an insufficient amount of royalties under the contract, and that the breach by the Secretary of its fiduciary duty to enforce the leases did not excuse the lessees from subsequently having to pay the amounts determined to be owed under the leases, citing *Atlantic Richfield Co. v. Hickle,* 432 F.2d 587, 592 (10th Cir. 1970). (Pet. Jt. App. 18a-19a).

STATEMENT OF FACTS

The Jicarilla Apache Tribe is an Indian Tribe organized and incorporated under the Indian Reorganization Act of June 18, 1934, 25 U.S.C. §§476-477, residing on an Executive Order Reservation in Rio Arriba and Sandoval Counties in northern New Mexico.

The leases which are the subject of litigation were issued pursuant to the Indian Mineral Leasing Act of May 11, 1938, 25 U.S.C. §§ 396a-396g. (Pet. Jt. App. 200a). The applicable regulations are contained in 25 C.F.R. Part 211 (1985) (formerly 25 C.F.R. Part 171) (Pet Jt. App. 214a)

and 30 C.F.R. Part 221 (1982). (Pet. Jt. App. 238a). The standard lease form issued pursuant to the 1938 Act is shown at Pet. Jt. App. 377a.-386a.

A. The History of the Gas Purchase Contracts and the Dealings of the Parties.

It is particularly important to note, from Plaintiff's Exhibit "5" (Resp. App. A), which is a summary of lease assignments and gas purchase contracts, that all of the leases in suit excepting lease 47 were issued either originally to SUG or its then wholly-owned subsidiaries, Southern Union Production Company (Supron) or Aztec (now Southland). Lease 47 was assigned to SUG shortly after its issuance. SUG assigned a separate undivided one-half interest in Leases 104 and 107 to Humble Oil Company (later Exxon). On January 2, 1984, SUG entered into a lease purchase option agreement to assign separate undivided one-half interest in Leases 100, 103, 105, 106, 145 and 153 to Aztec (later Southland), at that time a wholly-owned subsidiary of SUG. SUG contracted to buy gas from these leases on December 12, 1953 *before Aztec acquired any interest in the leases involved.* The other half interest in Leases 10, 47, 100, 101, 103, 104, 105, 106, 107 145, 150 and 153, was assigned on January 1, 1961 to SUG's other wholly-owned subsidiary SUPC (later Supron). On the same date purchase contracts to purchase gas for the life of these leases were entered into between SUG and SUPC. *See* District Court Opinion, Pet. Jt. App. 106a-107a. Leases 397 and 416 were acquired by Aztec in 1966 and 1969, respectively, while Aztec was a wholly-owned subsidiary of SUG. Gas from these leases was contracted to SUG pursuant to amendment of the December 12, 1953 gas purchase contract with Aztec. SUPC acquired Leases 417 and 418 on May 18, 1969. Purchase of gas from these leases was contracted to SUG by contracts dated December 12, 1953. These lease dates and assignments are shown on the chart, Pl-Exh-5, Resp. App. A. These contracts between SUG and it subsidiaries fixed price schedules for

intrastate gas purchases by SUG in the San Juan Basin, which was still used by SUG for gas sold on the reservation for royalty payments to the Tribe until 1976, when the Supervisor U.S.G.S. wrote to certain producers setting minimum prices for royalties to be paid to the Tribe. Pet. Jt. App. 179a.

It is clear, as a result of the corporate interrelationship of the oil companies, that these lease assignments, gas purchase contracts, and the later gas processing agreements between SUG, SUPC and Southern Union Refining Company, were not arms-length agreements.

As stated by Judge Seymour, the interpretation by the majority panel of the Tenth Circuit Court of Appeals of the royalty accounting obligation would permit the parties to fix royalties at a low figure without recourse for the Tribe or the Secretary. (Pet. Jt. App. 48a).

Whether the relationship and actions of these affiliated companies constituted violations of the antitrust laws or not as found by the District Court, it is abundantly clear that SUG by reason of its control of the market and affiliation with major producers was able to fix prices and enter into arrangements for processing which enabled SUG, Supron and Aztec to profit directly or indirectly from extraction and sale of liquids without paying commensurate royalties to the Tribe.

Southern Union Refining Company, which took over the Lybrook Extraction Plant from Supron at the end of 1976 was initially a wholly-owned subsidiary of Supron and remained a subsidiary of SUG during periods relevant to this case. The relationship of these affiliated companies is outlined in the testimony of Mr. Jack Hertz, Vice President of GCNM. (*See* Resp. App. B).

Resp. App. C shows that not only were prices paid producers by SUG for gas produced from Jicarilla leases lower than the New Mexico average prices, but they were

substantially lower than Federal Power Commission ceiling prices in the years 1971, 1972 and 1973. As the Federal Power Commission stated in its Opinion 658, dated April 11, 1973, Resp. App. D, producer bargaining in the Rocky Mountain area was less effective than elsewhere in the country and that the structure of the buyer segment could well have a regressive impact on exploration and development. As noted by the Commission, the lack of competition in gas purchasing was the primary reason for the low prices prevailing in the San Juan Basin.

B. The Liquids Processing Contracts Benefited SUG and Supron, but No Royalties Were Paid to The Tribe.

SUG built the Lybrook Plant in the 1960's; Supron acquired ownership of the plant in exchange for stock issued by SUG. The original processing agreement entered into January 1, 1971 provided for a ten percent processing fee payable to SUG by Supron. The contract allowed processing of all intrastate natural gas, with gas from the east gathering system being processed at the Lybrook Plant and gas from the west gathering system being processed at the Huerfano Plant. (Resp. App. E.,) A later amendment entered into on May 1, 1972 provided for a 33 1/3% processing fee. (Resp. App. F.) SUG retained the rights to the gas and Supron to all the liquids extracted from gas. There was no provision for payment of royalties to the Tribe for the liquids extracted or for SUG's processing fee, although SUG was the original lessee of most of the leases. Originally there was no provision in SUG's gas purchase contracts for payment to any producers for liquids.

When the original gas purchase contracts were entered into, Aztec (Southland) was a wholly-owned subsidiary of SUG. All these petitioners, except Exxon, benefited from the earnings of SUG and Supron on liquids. Supron argued that although it may have been obligated to account for liquids prior to 1976, it should be relieved of that obligation

after 1976, by the simple process of conveying the plant to another affiliated company.

C. The Applicable Provisions of the Leases, Statutes and Regulations.

All the leases subject to this litigation were issued pursuant to the Indian Mineral Leasing Act of May 11, 1938, 25 U.S.C. §§ 396a-396g. Section 4 of that Act, 25 U.S.C. § 396d provides:

> All operations under any oil, gas, or other mineral lease issued pursuant to the terms of sections 396a to 396g of this title or any other Act affecting restricted Indian lands shall be subject to the rules and regulations promulgated by the Secretary of the Interior. In the discretion of the said Secretary, any lease for oil or gas issued under the provisions of sections 396a to 396g of this title shall be made subject to the terms of any reasonable cooperative unit or other plan approved or prescribed by said Secretary prior or subsequent to the issuance of any such lease which involves the development or production of oil or gas from land covered by such lease. (Pet. Jt. App. 201a.)

The leases in this suit were executed in the early 1950's, and the regulations then in effect have not changed since that time in any material respect. The lease form and the regulations clearly vest discretion in the Secretary to determine "value" for computation of royalty. This discretion, as the trial court held and Judge Seymour's opinion clearly demonstrates, is circumscribed by the Secretary's fiduciary obligation to the Tribe.

Paragraph 3(c) of the Standard Lease (Pet. Jt. App. 377a) provides that the royalty at the applicable percentage be computed on "the value or amount of all oil, gas and/or natural gasoline, and/or all other hydrocarbon sub-

stances produced and saved from the land leased herein. . . ."

The lease provides that the Secretary has discretion to ascertain "value" for the computation, and provides further (paragraph 3(c));

> During the period of supervision, "value" for the purposes hereof may, in the discretion of the Secretary, be calculated on the basis of the highest price paid or offered (whether calculated on the basis of short or actual volume) at the time of production for the major portion of the oil of the same gravity, and gas, and/or natural gasoline, and/or all other hydrocarbon substances produced and sold from the field where the leased lands are situated, and the actual volume of the marketable product less the content of foreign substances as determined by the oil and gas supervisor. The actual amount realized by the lessee from the sale of said products may, in the discretion of the Secretary, be deemed mere evidence of or conclusive evidence of such value.

The regulations, 25 C.F.R. § 211.13 (1985) (formerly § 171.13) (Pet. Jt. App. 214a), contain an identical provision for determining "value." 30 C.F.R. § 221.47 and § 221.50 (Pet. Jt. App. 238a) reinforce a conclusion that the Secretary has discretion to determine value based on the highest price paid for a part or a majority of like quality of oil or gas in the same field, and that the Secretary has the obligation to include the value of liquid products in determining royalty, whether these liquid products are extracted by the lessee or by others. The analysis of the applicable lease provisions and regulations are set forth below, pp. 19-23.

REASONS FOR DENYING THE WRIT

ARGUMENT

I. THE SECRETARY'S REQUIREMENT OF DUAL ACCOUNTING AND DETERMINATION OF VALUE WAS REASONABLE UNDER STANDARDS OF ADMINISTRATIVE LAW AND REQUIRED BY HIS FIDUCIARY OBLIGATION.

A. The Secretary Has a Broad Fiduciary Obligation to the Tribe Which Mandates a Determination of Value Independent of Proceeds to Lessees.

Title 25 U.S.C. § 396d (Pet. Jt. App. 201a) quoted above has direct application to the case at hand. This statute confers on the Secretary the authority to promulgate regulations governing operations pursuant to the leases and expresses a congressional policy of establishing a fiduciary relationship in which the particular duties of the trustee and the rights of the beneficiary are delineated. All Jicarilla Apache Tribal lands are held by the United States in trust for the Tribe.

Section 396d clearly establishes a fiduciary obligation on the part of the Secretary, not only to promulgate rules and regulations, but also to *administer* such rules and regulations. Thus, the Tribe contends that the Secretary has a fiduciary duty under § 396d to *enforce* the regulations promulgated under that section. To claim otherwise would be to make a mockery of the acts and the intent of Congress.

In *Kenai Oil & Gas, Inc. v. Dept. of Int. of U.S.*, 671 F.2d 383 (10th Cir. 1982), the Tenth Circuit Court reviewed the fiduciary role of the Secretary of the Interior and his delegates, in the context of the Secretary's trust responsibility for the approval of communitization agreements pursuant to 25 U.S.C. § 396d. In holding that the Secretary or his delegate could not be compelled to approve communitization agreements which would extend

non-productive leases beyond their primary term, the Tenth Circuit Court said: "As a fiduciary for the Indians, the Secretary is responsible for overseeing the economic interest of Indian lessors, and has a duty to maximize lease revenues." *Id.* at 386. The Secretary's construction of regulations and exercise of discretion is "limited by the fiduciary responsibilities vested in the United States as trustee of Indian lands." *Id.* at 386. The Court said further:

> Furthermore, limiting the Superintendent's considerations solely to matters of conservation and production would be inconsistent with his trust responsibilities to the Indians in leasing tribal lands. In light of these trust responsibilities, the Superintendent must take the Indians' best interests into account when making any decision involving leases on tribal lands, and has broad discretion to consider all factors affecting their interests.

Id. at 387. Thus, just as a limitation on the discretion of the Secretary or his delegate in approving communitization agreements would be inconsistent with the Secretary's trust responsibilities, limiting the Secretary's obligation in determining "value" would also be inconsistent with his trust responsibilities.

The purpose of the 1938 Indian Mineral Leasing Act and congressional policy is to obtain the maximum benefit from oil and gas for Indian tribes. The Secretary has a fiduciary obligation to secure this maximum benefit to the tribes. If the Secretary has discretion in administering law and regulations and supervising operations under Indian leases, this discretion must be exercised in light of his fiduciary obligation. If there is more than one "reasonable" choice, as that term is used in administrative law, the Secretary must choose that which is to the best interest of the Tribe.

In the instant case, the Secretary belatedly recognized his fiduciary obligation, both as to determination of value and enforcement of dual accounting, after the demands made by the Tribe and pursuant to the order of the District Court. As is shown in Point B below, there was no prior inconsistent interpretation by the Department—only a long history of inaction in enforcing the provisions of Indian leases and applicable regulations.

Neither the history of administration of the Indian Mineral Leasing Act and regulations, nor the holdings of this Court, are inconsistent with a determination of value which is independent of the price paid or proceeds to the lessee. Thus, the Circuit Court of Appeals for the Tenth Circuit in *Hoover & Bracken Energies, Inc. v. Department of Interior,* 723 F.2d 1488 (10th Cir. 1983), held that royalties were not limited by price paid to the producer, but had to be paid on price plus state severance taxes, even though Indian and federal production were not subject to these state taxes. Petitioners would limit value for payment of royalties to the price paid.

In *United States v. Mitchell* (*Mitchell II*), 463 U.S. 206 (1983), this Court recognized that the timber management statutes established comprehensive responsibilities of the federal government in managing the harvesting of Indian timber, and noted that the government recognized its duties in managing Indian forests so as to obtain the greatest revenues for the Indians consistent with a proper protection and improvement of the forest. Similarly, the Indian Mineral Leasing Act established comprehensive responsibilities in the federal government which give rise to a like obligation to manage tribes' oil and gas resources to obtain the greatest revenue for the Indians consistent with proper protection and improvement of their lands.

The *Report of the Commission on Fiscal Accountability of the Nation's Energy Resources* (U.S.G.P.O. 1982) led to the enactment of the Federal Oil and Gas Royalty Man-

agement Act of 1982 (codified at 30 U.S.C. §§ 188, 191, 1701, 1702, 1711-1723, 1731-1736, 1751-1757 (1986)). In Section 2 of the Act, Congress recognized that the system of accounting with respect to royalties and other payments due on oil and gas produced from federal and Indian lands was archaic and inadequate. The Act stated that it was essential that the Secretary initiate procedures to improve methods of accounting for royalties and to provide for routine inspection of activities related to the production of oil and gas on lease sites. The Act specifically stated that one of its purposes was to "fulfill the trust responsibility of the United States in the administration of Indian oil and gas resources". Section 101(b)(c)(1) required the Secretary to audit and reconcile, to the extent practicable, all current and past lease accounts for leases of oil or gas and take *appropriate actions to make additional collections or refunds as warranted.*" (emphasis added)

It would obviously subvert the purposes and objectives of the Royalty Management Act if the Secretary were bound by previous failures to enforce Indian lease terms or regulations, or if his discretion were so limited that he could not insure that tribes receive the maximum income from the development and exploitation of their resources. Thus, the real issue in this case is whether given two reasonable interpretations, the Secretary's trust responsibilities require him to apply whichever accounting method (Btu or net realization) yields the Tribe the greatest royalty.

B. The Secretary Made No Determination of Value or Interpretation of Law and Regulations as to Dual Accounting Prior to the Tribe's Demand.

Petitioners mistake *inaction* and failure of the Secretary to enforce existing regulations under the mineral leasing laws for a positive administrative interpretation of the regulations and leases. The record is devoid of any evidence of an administrative interpretation to the effect that

"value" equals "proceeds", or that liquids accounting was required only of lessees who operated extraction plants. It is true that lessees who did not operate liquids extraction plants had not previously been required to account for liquids. However, it is also true that no lessees on the Jicarilla Apache Reservation, including those operating extraction plants, had ever been required to account for liquids by action of the Secretary.

The failure of the Department of the Interior to monitor and audit royalties, either for value or for liquids accounting, was made clear by the *Report of the Commission on Fiscal Accountability of the Nation's Energy Resources, supra,* transmitted January 21, 1982 to Secretary of the Interior Watt. This report underscored the vital importance to the Nation of full and correct payment of royalties and the long-standing failure of the Department of Interior to monitor or audit royalty payments on federal or Indian lands.

Prior to 1973, when the Tribe made demands on the Secretary to enforce lease provisions on the reservation, there had essentially been no monitoring or auditing of royalty payments to the Tribe. In a letter of President Hubert Velarde of the Tribe dated June 29, 1973 to the Secretary, the Tribe pointed out that royalties were being paid on artificially maintained low prices; that no royalties were being paid on liquids; and that the Department was failing to enforce other provisions of the leases. (Resp. App. G). On July 29, 1974, a letter was written by the Commissioner of Indian Affairs to the Secretary, asking the U.S.G.S. to provide the Tribe with information as to the true value of oil and gas produced on the reservation from 1953 to the present which should be used in royalty computations, the by-products and amounts thereof derived from the subject production, the cost of manufacture of the above-named by-products and the value of the above by-products. (Resp. App. H). The Department established a "Jicarilla Response Committee" in August, 1974, to re-

spond to the Tribe's demands. The Jicarilla Response Committee obtained cost data on the manufacture on the extraction of liquids and compared the Btu adjustment prices against net realization prices (net realization value equals the value of liquids extracted less cost of manufacture, plus the value of residue gas at the tailgate of the extraction plant). The Response Committee, in its various bi-weekly reports of activities to the Chief of the Conservation Division, U.S.G.S., continued to maintain that the net realization value of natural gas liquids was not as advantageous to the Tribe as the Btu adjustment method.

In 1975, because of the increased market price of extracted liquids, it became apparent that the net realization method would yield a higher value than the Btu adjustment method if actual cost of manufacture were used. Accordingly, at various times on or after December 9, 1976 the Area Oil and Gas Supervisor, U.S.G.S., issued letters to SUPC requiring SUPC to file corrected monthly reports of sale and royalty for 1974, 1975 and 1976 to date to show both Btu and net realization methods of reporting royalty. The corrected reports indicated substantial underpayments and SUPC paid substantial sums to the Tribe in additional royalties based on liquids accounting. *See* I.B.L.A. Opinion (Pet. Jt. App. 179a-180a).

At about the same time, a letter was sent to the Department of the Interior by the Albuquerque Area Office, asking for a determination as to whether producers whose gas was processed though plants which they did not own, would be required to account for liquids. As of the date of trial in the District Court, no decision had been received from the Secretary. *See* Opinion of the District Court (Pet. Jt. App. 133a).

The District Court found that until 1974, producers selling natural gas to SUG were paid a base contract price, plus a penny per Mcf, which they claimed presumably satisfied any obligation that producers had to account for

liquids in the gas stream. From 1974 on, producers received a Btu adjusted price for gas sold to SUG without any additional amount paid for liquids. The Court concluded that the Secretary was required to have producers account to the Tribe by the dual accounting method if gas produced from the lease is processed into component products, whether or not the particular producer owned and operated an extraction plant. (Pet. Jt. App. 132a).

It is thus clear from the record that there was no positive administrative construction or interpretation of the Secretary's obligation to determine value or to require producers to account by the dual accounting method until the Tribe's complaints were received.

C. The Secretary Of The Interior Cannot Be Bound By a Prior Interpretation of "Value" That Did Not Exist.

In *Supron Energy Corp., et al.*, 46 I.B.L.A. 181 (1980) (Pet. Jt. App. 176a-199a), the Interior Board of Land Appeals considered the contention of the oil companies that the Department of Interior, by accepting the companies' monthly reports, had exercised its discretion in determining "value" for royalty purposes. In deciding against the oil companies, the Board found that the Department did not accept the actual sales price as representative of "true value", and that the Department's *first* action to determine "value" was made by the Area Supervisor as a result of this case. The Board explained the practice of billing lessees for royalty on the basis of monthly statements which stated value as sales price, *subject to post audit.* There was no verification by GS personnel as to value.

Likewise, the Oil and Gas Supervisor has now exercised his discretion to determine that "value" on royalties will be calculated by submitting his final accounting to the Court. To successfully override the Secretary's determination of value, Petitioners must submit evidence that he acted in an arbitrary and capricious manner. No such evi-

dence has yet been presented. In fact, the majority opinion of the three-judge panel of the Circuit Court found there was no arbitrary or capricious action, yet overturned the determinations of the Secretary. Such an administrative interpretation by the Department of its own regulations should be given controlling weight unless plainly erroneous or unless it is inconsistent with the regulations. *Udall v. Tallman,* 380 U.S. 1 (1965), *reh. denied,* 380 U.S. 989 (1965); *Immigration & Naturalization Service v. Stanisic,* 395 U.S. 62 (1969), *reh. denied,* 395 U.S. 987 (1969). Petitioners cite *Continental Oil Company v. United States,* 184 F.2d 802, (9th Cir. 1950) for the proposition that the Department cannot reassess royalty value in excess of a previously determined value billed by the Department. *Continental* does not support Petitioners' position, as held by the Indian Board of Land Appeals. In *Continental* the Department had previously issued an order determining value. In this case there had been no such earlier interpretation.

D. The Oil Companies Were Correctly Required to Employ Dual Accounting In Order To Determine Value Under The Leases And The Regulations.

The District Court, in its Memorandum Opinion of November 5, 1979, 479 F. Supp. 536 (1979), concluded "that where, as here, gas produced from the lease is processed into component products, dual accounting is required by the terms of the lease." 479 F. Supp. at 551. (Pet. Jt. App. 131a). This conclusion was consistent with the subsequent independent conclusion of the Interior Board of Land Appeals in *Supron Energy Corp., et al., supra.* with respect to Supron. In that case, the Department held that paragraph 3(c) of the lease clearly requires that the lessees employ dual accounting to determine the value for royalty accounting purposes. The board also determined that the Btu adjustment method was justified by 30 C.F.R. § 221.47, and that the net realization method was justified by 30

C.F.R. § 221.50. (Pet. Jt. App. 261a-264a). Given the independent, though parallel, conclusions of the District Court and the Interior Board of Land Appeals, the weight of that authority clearly indicates that dual accounting by lessees is required under the terms of the lease and the regulations. Further, the Department of Interior's interpretation of its own regulations and lease forms should be given controlling weight. *Udall v. Tallman, supra.*

The oil companies cite the last sentence in 30 C.F.R. § 221.47 for the proposition that the "highest price paid or offered" must be accepted as value for royalty purposes, but they ignore the language of the first sentence, which reads as follows:

> The value of production, for the purpose of computing royalty shall be the estimated reasonable value of the product as determined by the supervisor, due consideration being given to the highest price paid for a part or for a majority of production of like quality in the same field, to the price received by the lessee, to posted prices and to other relevant matters.

More importantly, they ignore the second sentence of § 221.47, which reads as follows:

> Under no circumstances shall the value of production of any of said *substances* for the purposes of computing royalty be deemed to be less than the gross proceeds accruing to the lessee from the sale thereof *or less than the value computed on such reasonable unit value as shall have been determined by the Secretary.* (emphasis added)

The "substances" referred to above are those listed in § 221.46: "Casinghead or natural gasoline, butane, propane, or other liquid hydrocarbon substances extracted from gas. . . ." Thus, the computation of liquids royalty employing the "value basis" in § 221.47, includes the value

of "liquid hydrocarbon substances" whose value is no less than the "gross proceeds", i.e. sales price, accruing to the lessee, or no less than the "reasonable unit value", i.e. price per gallon or Mcf, as determined by the Secretary. Of course, Supron did extract liquids when it owned the Lybrook Plant, but never accounted for any royalties from plant profits until ordered to do so by the Oil and Gas Supervisor and finally the Court. The facts reveal that when all of the gas purchase contracts were executed, without reserving processing rights, that the sales contracts were made with the companies' parent company, SUG, (except for Exxon) which owned the Lybrook Plant, and that the oil companies' leases were originally held by SUG. Even the majority opinion in the original Tenth Circuit decision apparently requires dual accounting of Supron as a plant operator.

In order for the value of liquids to be computed on such reasonable unit value the *quantity* of liquids must be determined under 30 C.F.R. § 221.46 (Pet. Jt. App. 260a). This section vests broad discretionary authority in the Supervisor to make such determination, and provides for the use of two basic methods. The first method involved the allocation of the "net output" (i.e., "the quantity of each substance that the plant produces for sale") of the products produced from each leasehold by taking into account the "gasoline content" (§ 221.46(b) & (c)) or individual hydrocarbon content (§ 221.46(d)) and the number of leases involved. The second method (§ 221.46(e)) involves the estimation of liquid hydrocarbon production when the first method is not "practicable", *in the judgment of the Supervisor*, by taking into account the "quantity of gas produced from the leasehold and transmitted to the extraction plant", a test for individual hydrocarbon content, and the efficiency of the plant. Further, the Supervisor's estimation of "quantity" under the second method is "determined as to *insure full protection of the royalty interest of the lessor*" (emphasis added), which clearly indicates that this

method must be employed where in the judgment of the Supervisor, the proper and accurate valuation of liquids royalty cannot be otherwise determined or where the royalty interest of the federal or Indian lessor would in effect be diminished or circumvented. Reading § 221.46 in the context of § 221.47, the royalty value for liquid hydrocarbons is calculated by either (1) computing the quantity and unit value of those liquids as determined by the Supervisor and the Secretary or (2) taking the gross proceeds or actual amount realized by a lessee who sold the liquids for extraction.

The method of computation of value for "wet gas" (gas and entrained liquids) under § 221.50(c) (Pet. Jt. App. 265a) is identical with that used for the computation of liquids value under § 221.47, which indicates the comprehensive and compatible scheme of valuation in royalty accounting embodied in the regulations. Section 221.50, in the context of the comprehensive regulatory scheme in Part 221, reveals that it addresses the two basic situations encountered by a lessee producer: subsections (a) and (b) apply where a lessee-producer sells the gas and liquids as components directly to a gas purchaser and a component product purchaser or where the lessee-producer processes the gas and components himself; and, subsection (c) applies where, as is the usual case, a lessee-producer sells the gas and liquids as "wet gas". A lessee-producer who sells "wet gas" under § 221.50(c) is *expressly required* to perform dual accounting in order to determine "whichever is greater". Under both regulations and the provisions of paragraph 3(c) of the lease, dual accounting is required, and the value of liquid hydrocarbons must be included in such accounting. Thus, the District Court, the Interior Board of Land Appeals and Judge Seymour were consistent in their interpretations of that section.

The majority of the panel of the Tenth Circuit Court also mistakenly construed the words "produced and sold from the field" as meaning produced and sold from the

leased lands, thus concluding that royalties need be paid only on liquids processed on the leased lands by the lessee.

This latter construction of "field" is contrary to the common sense construction of the word used by industry and by the Supervisor. Thus, the Area Oil and Gas Supervisor in Albuquerque, in determining whether additional royalties should be assessed against these oil companies to determine the highest price paid for the majority of gas produced and sold from the field for the years 1971 through 1973, assembled complete gas sales data on all Jicarilla Apache tribal leases, including those selling to interstate purchasers. He determined the median price for all gas from these leases and adopted these median prices as the *floor* values for each year. The Interior Board of Land Appeals held that this was in the discretionary latitude granted to the Supervisor by the regulations. (Pet. Jt. App. 185a).

The Petitioners erroneously contend that dual accounting should not be required and royalty should not be paid for liquids on their production either because they did not receive any benefit from the liquids or because the liquids processing plant owner has no legal obligation to provide the data they need for dual accounting. The lessee-producers' claims that they received no benefit or proceeds from the liquids ignores the fact that they agreed to the gas purchase contract which allowed SUG to take the liquids without compensation. They could have sought relief from the restrictive contract provisions either through negotiation or through the courts. Nevertheless, their contracts with SUG or GCNM relieve the lessee-producers of the incidence of liability for payment of additional royalties resulting from dual accounting by providing that "excess royalty payments" be reimbursed by SUG or GCNM. If the lessee-producers could not, for any reason, obtain from the processing plant the data required for dual accounting, then the supervisor's estimation pursuant to 30 C.F.R. § 221.46(e) would be additionally justified and would be

substituted for the unobtainable data for the purpose of dual accounting. The claims of the producing companies of actual injury to them as innocent parties is belied by the reimbursement provisions of their contracts with SUG, the party which profited substantially form the additional values secured by extraction of liquids.[1]

E. The Leases Require Royalties to be Paid on Market "Value".

The royalty clause of the standard BIA lease is a typical "market value" clause. Nonetheless, Petitioners construe the royalty clause to require that royalties be paid on the "net proceeds" to the lessee. The courts throughout the United States have long recognized the difference between "market value", "market price" and "net proceeds" royalty clauses. Proceeds and market value are distinguished in *Waechter v. Amoco Prod. Co.,* 537 P.2d 228, 249 (Kan. 1975), *on rehearing,* 546 P.2d 1320 (1976); and in *Lightcap v. Mobil Oil Corp.,* 221 Kan. 448, 562 P. 2d 1, *cert. denied,* 434 U.S. 876 (1977). *See generally,* Williams and Meyers, *Oil and Gas Law,* § 650.2.

This Court should continue to recognize these distinctions and not substitute judicial interpretations for the plain meaning of the lease clause.

ARGUMENT

II. THE DECISION OF THE COURT OF APPEALS IS NOT IN CONFLICT WITH ANY COURT OF APPEALS DECISION NOR ANY DECISION OF THE SUPREME COURT

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[1] The Reimbursement provisions of the contracts between the Gas Company of New Mexico and Petitioners are the basis for judgments by Petitioners against Gas Company of New Mexico and are quoted in the District Court's Memorandum Opinion of June 1, 1981. Pet. Jt. App. 165a-172a.

A. The Decision Does Not Conflict With This Court's Decisions in *Mountain States Telephone and Telegraph Company v. Pueblo of Santa Ana* and *Nevada v. United States.*

Petitioners cite *Mountain States Telephone and Telegraph Company v. Pueblo of Santa Ana,* 105 S. Ct. 2587 (1985) and *Nevada v. United States,* 463 U.S. 110 (1983) as decisions that conflict with the Tenth Circuit decisions in this case. In the *Mountain States* decision, this Court's reversal of the Tenth Circuit's affirmance of a District Court decision setting aside a BIA administrative interpretation was based on the reasoning that the executive officials implementing the Pueblo Lands Act of 1924 were more likely to have an understanding of the actual intent of Congress than judges who must consider the legal implications of the transaction over half a century after it occurred. Petitioners equate this reasoning to Judge Seymour's reasoning and the reasoning of the District Court but fail to recognize that in this case there was no long-standing administrative interpretation. *Mountain States* has no application to a case such as this where the courts as well as the Congress have recognized long-time inaction and failure to enforce lease provisions that have acted to the detriment not only of Indian tribes but of the federal government and of states.

In *Nevada v. United States* relied upon by Petitioners, the tribe's claims against third parties was held barred because the tribe's water rights had been previously adjudicated in a 1913 Federal District Court decree. The third parties in *Nevada* were "thousands of small farmers in northwestern Nevada" who had "specific promises made to their forebearers two or three generations ago." 463 U.S. at 145. (Brennan concurring). Those small farmers had no relationship to the tribe in that case. In contrast, the third parties in this litigation are energy companies who had agreed to lease provisions reasonably susceptible to the interpretation that royalties be based on the highest

value reasonably obtainable under their lessees. In this case the Petitioners merely misinterpreted lease provisions and the Secretary failed to act to enforce these provisions.

B. The Decision is Consistent with the Decision of the Ninth Circuit Court of Appeals in *Marathon Oil Company v. United States*, the Only Other Court of Appeals Case Decided on the Same Issue.

In the recent decision of the Court of Appeals for the Ninth Circuit, *Marathon Oil Company v. United States*, 794 F.2d 1461 (9th Cir. 1986), the Ninth Circuit Court of Appeals concurred with the Court of Appeals for the Tenth Circuit in affirming the Secretary's authority to interpret the royalty provisions of natural gas leases derived from the Mineral Lands Leasing Act, 30 U.S.C. § 181 *et seq.*, That Act and the Act in question grant broad powers to the Secretary. The Mineral Land Leasing Act authorized the Secretary to "prescribe necessary and proper rules and regulations and to do any and all things necessary to carry out and accomplish the purposes of (the Act)." 30 U.S.C. § 189. Years after the leases were executed in *Marathon*, the Secretary determined the royalties should be computed on a net back formula rather than the price paid for gas at the wellhead. In the instant case, the Secretary similarly determined that royalties should be computed on a net-realization formula rather than on the price paid for gas at the wellhead, provided that the net-realization formula resulted in the highest payment to the Tribe. The Secretary's interpretation in *Marathon* was also applied retroactively, as in this case.

The decision of the Court of Appeals in this case is in accord with principles of federal trust responsibility that have long been articulated by this Court. There is no real conflict between the decisions of the Court of Appeals in this case and this Court's decisions in *Mountain States* and *Nevada*. The Tenth Circuit decision in this case is supported by the decision of the Ninth Circuit in *Marathon*.

There is thus no important question of federal law which has not but should be settled by this Court, nor has a federal question been decided in this case in a way that conflicts with any decisions of this Court.

ARGUMENT

III. THE COURT SHOULD DENY THE WRIT BECAUSE THE QUESTIONS OF FEDERAL LAW ARE BASED ON PECULIAR FACTS INVOLVING ONE INDIAN RESERVATION AND ARE NOT OF IMPORTANCE TO THE NATION AS A WHOLE.

A. There are No Special or Important Reasons to Grant the Writ.

This court has noted that the "special and important reasons" referred to in Supreme Court Rule 17 must be of importance to the nation as a whole to invoke the discretionary review of this Court. *Rudolph v. U.S.*, 370 U.S. 269, 270, (1962) (Writ of Certiorari dismissed as improvidently granted because "review would be of no importance save to the litigants themselves.") In *Rice v. Sioux City Cemetery*, 349 U.S. 70 (1955), the Court originally granted certiorari to consider a contract prohibiting burial of non-Caucasians in an Iowa cemetery. After the dispute arose, the Iowa legislature passed corrective legislation that prevented a similar situation from occurring again. 349 U.S. at 73. The legislation did not apply to parties in litigation at the time of the enactment; therefore, the issue was still of importance to the parties who had petitioned for certiorari. 349 U.S. at 76. Nevertheless, the court dismissed the writ as improvidently granted, stating that "It is very important that we be consistent in not granting the writ of certiorari except in cases involving principles the settlement of which is of importance to the public as distinguished from that of the parties. . ." 349 U.S. at 79 quoting Layne & Bowler Corp. v. Western Well Works, Inc., 261 U.S. 387, 393 (1923). There are no special and

important reasons to grant the Writ in this case, for the reasons stated below.

B. Remand of This Case Would Not be Cost Effective Because a Large Part of Additional Royalties Assessed Were Based on Values in Excess of New Mexico Statutory Price Ceiling and the New Mexico Act has Terminated.

The situation in this case is similar to that in *Rice v. Sioux City Cemetery, supra.* A substantial amount of additional royalties assessed against Petitioners were based on the difference between the ceiling price of natural gas established by the New Mexico Natural Gas Pricing Act of 1978, N.M. Stat. §§ 62-7-1, *et seq.* (NMGPA) and the prices upon which Petitioners based their royalty payments. The prices paid to producers for natural gas for intrastate natural gas in New Mexico were lower than prices prevailing on interstate gas. The District Court held that the New Mexico Legislature had not intended the Act to apply to royalties paid the Tribe and that the Secretary in determining "value" should have established value for royalties paid to the Tribe not limited by the NMGPA. The NMGPA terminated effective June 30, 1985. Chapter 123 N.M. Session Laws 1984 § 15. Petitioners have not requested review as to this portion of the District Court's decision. In the event this case is remanded to the District Court for reaccounting, both the Secretary and the Petitioners would be confronted with an expensive reaccounting, to determine whether the additional royalties paid pursuant to the District Court's judgment were based on dual accounting or on the limits imposed by the NMGPA. Moreover, this reaccounting, in the event that it resulted in partial repayment by the Tribe of additional royalties heretofore paid by the companies (*see* Attachment A to Appellant's Motion to Require Appellees to File Additional Bond or Other Security), (Resp. App. I) would result in payment to Public Service Company of New Mexico and would presumably require proceedings before the Public

Service Commission of New Mexico to determine whether reimbursement to customers of PNM would be required. The cost of these proceedings would in all probability exceed any possible benefits obtained by PNM or Southern Union Company as a result of a remand of this case.

The question also arises as to the effect of the Stipulation for Settlement between Gas Company of New Mexico and the Tribe entered into October 21, 1976. Paragraph one of this Stipulation recites as follows:

> 1. The Tribe and GCNM have entered into a Settlement Agreement, a Royalty Gas Gathering Agreement and a Royalty Gas Purchase Contract, all of even date herewith settling other matters in dispute between the Tribe and GCNM, which Agreements are incorporated herein by reference.

Paragraph 8 of the Stipulation provides as follows:

> 8. All matters in controversy in this case between the Tribe and Defendants GCNM and Southern Union Gathering Company having been settled, the parties hereto request the Court to enter this Stipulation as its final judgment in this case, and the case shall be dismissed with prejudice in its entirety as to GCNM and Southern Union Gathering Company, each party to bear its own costs.
>
> (Resp. App. J)

The District Court stated in its November 5, 1979 Opinion in footnote 2, Pet. Jt. App. 113a, that while evidence revealed that SUG tended to negotiate gas purchase contracts on a "take it or leave it" basis with regard to prices dictated by it, "this at best tends to reveal monopolistic activities attributable not to defendant-lessees, but to SUG, who has bought its peace in this lawsuit. This apparently illegal activity on the part of SUG cannot be imputed to

the defendants remaining in this action." (Pet. Jt. App. 113a, fn.2).

SUG after settling with the Tribe then rejoined the case and is attempting to reach the Tribe through the back door by recovering the monies it has agreed to pay the other Petitioners pursuant to the excess royalty reimbursement contracts with these Petitioners.

C. The Department of Interior is Currently Revising Its Regulations for Determination of the Value of Gas.

On July 25, 1986 the Department of Interior, Minerals Management Service (MMS) published a Notice of Modification to Notice To Lessees Number 5 (NTL-5) entitled "Procedures for Determining Natural Gas Value for Royalty Purposes". The stated purpose of the changes was "to permit MMS to value most natural gas by using the full range of its authority under the royalty valuation regulations in 30 C.F.R. rather than the more restrictive provisions of NTL-5." 51 F.R. 26759. On August 9, 1977 because of questions raised by the Tribe as to the supervision of royalty accounting on Tribal production, and the failure of the U.S.G.S. independently to determine value, the U.S.G.S. caused to be published an Order suspending the operation of NTL-5 to oil and gas leases on the Jicarilla Apache Reservation for an indefinite period as of June 1, 1977. 42 F.R. 40263, August 9, 1977. (Resp. App. K).

On February 5, 1986 the MMS published proposed rules entitled *Product Evaluation For Royalty Purposes.* (Pet. Jt. App. 341a-376a). In the background section of the Notice, it was stated that the Secretary had appointed a Royalty Management Advisory Committee comprised of thirty-one representatives from industry, the states and Indian tribes, which will have as one of its first tasks to advise the Secretary on the new product value regulations. The Advisory Committee held its first meeting in Lakewood, Colorado on January 9 and 10, 1986. It was stated in the Notice that the MMS had decided to make drafts

of the proposed regulations available for public review and comment before issuing formal notices of proposed rulemaking. It was made clear that the draft regulations set forth in the Notice were not final and would be subject to change after consideration of the recommendations of the Advisory Committee. (Pet. Jt. App. 341a-343a).

In view of the pending issuance of new regulations, the Court should not pre-empt the Department of Interior by interpreting existing regulations. The questions raised by Petitioners with respect to interpretation of the present regulations will be of no national importance in the future.

CONCLUSION

Respondent submits that the true purpose of Petitioners' and Amici's efforts to overturn the decision of the Court of Appeals for the Tenth Circuit on Rehearing is a thinly disguised attempt to prevent the Secretary in the future from auditing royalty payments made by these companies to Tribes and states, and to perpetuate past practices of accepting "net proceeds" as reported by producers as "value". The issues raised here pertain only to the Jicarilla Apache Reservation and are not of importance to the nation as a whole. There are, in reality, no issues raised which have not already been decided against the Petitioners in the Circuit Courts and in this Court.

Respectfully submitted.

ROBERT J. NORDHAUS
B. REID HALTOM
NORDHAUS, HALTOM, TAYLOR & TARADASH
507 Roma N.W.
Albuquerque, New Mexico 87102
Tel: 505-243-4275

Counel for Respondent
Jicarilla Apache Tribe

APPENDIX

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APPENDIX A

Summary—Lease Assignments and Gas I

(Plaintiff's Exhibit 5)

AZTEC OIL* (SOUTHLAND OIL)
1-1-55 ASSIGNED 100(1/2), 101(1/2), 103(1/2), 105(1/2), 106(1/2)
145(1/2), 150(1/2), 153(1/2), 12-17-66 ACQ. 397, 3-24-69 ACQ. 416

12-12-53

1950-72 100%

SOUTHERN UNION PRODUCTION CO.* (SUPRON)* 1972-76 71%, 1976-P
1-1-61 ASSIGNED 10, 47, 100(1/2), 103(1/2), 104(1/2), 105(1/2)
106(1/2), 107(1/2), 145(1/2), 150(1/2), 153(1/2), 5-18-69 ACQ. 417 AND 418

SOUTHERN UNION GAS CO.*
SOUTHERN UNION CO. *
GAS CO. NEW MEXICO *

1-1-61
HUMBLE OIL (EXXON)
5-20-52 ASSIGNED 104(1/2) AND 107(1/2)

CONSOLIDATED
8-12-64 ASSIGNED 106(1/2)

11-15-63, 12-4-63
TENNECO
9-1-64 ASSIGNED 108(1/4), 109(1/4), 110(1/4)

10-21-64
ATLANTIC (ARCO)
3-7-52 ASSIGNED 108(1/2), 110(1/2), 12-9-52 ASSIGNED 109(1/2)

DELHI OIL & GAS CO.*

10-21-64
CONTINENTAL
9-1-64 ASSIGNED 108(1/4), 109(1/4), 110(1/4)

10-21-64
PANAM (AMOCO) 10-3-61 ASSIGNED 102

HONOLULU OIL

10-25-56

SKELLY 198(1/2)

11-2-60

SINCLAIR 198(1/2)

11-23-60

Purchase Contracts

__ GAS PURCHASE CONTRACT SUG* (GCNM)*

RESENT 28½% O&G 100% GAS PROCESSING GAS PURCHASE CONTRACT SUG*

GAS PURCHASE CONTRACT SUG* (GCNM)*

GAS PURCHASE CONTRACT EL PASO NATL. GAS

GAS PURCHASE CONTRACT SUGC*

9-27-54

__ GAS PURCHASE CONTRACT SUG*(GCNM)*

GAS PURCHASE CONTRACT SUG*

__ GAS PURCHASE CONTRACT SUG*(GCNM)* GAS PURCHASE CONTRACT EL PASO

__ GAS PURCHASE CONTRACT SUG*(GCNM)*

__ GAS PURCHASE CONTRACT SUG*(GCNM)*

__ GAS PURCHASE CONTRACT SUG*(GCNM)*

__ GAS PURCHASE CONTRACT SUG*(GCNM)*

GAS PURCHASE CONTRACT SUG*(GCNM)*

GAS PURCHASE CONTRACT SUG*(GCNM)*

APPENDIX B

TESTIMONY OF MR. JACK HERTZ, VICE PRESIDENT OF GAS COMPANY OF NEW MEXICO (10 C.A. App. Vol. IV, A-639-642)

* * * * *

Q Now, Mr. Hertz, I'm still a little bit unclear about all these corporate relations. As I understand it, Southern Union Company is a Delaware corporation, is that right?

A Southern Union Corporation is a Delaware corporation.

Q And it operates a public utility business through two separate divisions?

A Yes. If I may, the company previously was Southern Gas Company. The Southern Gas Company owned utility operations in four states: Texas, Oklahoma, New Mexico and Arizona and April of 1976, the Board changed the name of Southern Union Gas Company to Southern Union Company, a Delaware corporation. Two public utility divisions were created; one, Gas Company of New Mexico, a Division of Southern Union Company, operating, owning and operating properties in New Mexico; and Southern Union Gas Company, a Division of Southern Union Company, owning and operating the natural gas public utility properties and in fact, a few water properties in Texas, Oklahoma and Arizona.

The two divisions were then of about equal size. The division concept of operation is certainly not unusual. The reason for creating divisions rather than subsidiary corporations is very basic. It's to avoid the complications of further requirements of the Public Utility Holding Company Act of 1975, which basically requires that any corporation that owns more than ten percent of the stock of a corporation engaged in the public utility business is subject to the Holding Company Act.

Q Now, as we're talking as of today, Gas Company of New Mexico is a Division of Southern Union Company and what was, and the name of Southern Union Gas Company belongs to another Division of Southern Union Company?

A That's correct.

Q There's no corporate relationship between Southern Union Company and Southland Royalty Company, is there?

A There is not now nor has there ever been.

Q And the only relationship between those two companies is the contractural relationship by virtue of the Natural Gas Purchase Contract that Southland succeeded to when it purchased Aztec?

A That's correct.

Q Now, would you explain what the business of Gas Company of New Mexico is?

A Gas Company of New Mexico is engaged in the natural gas public utility operation, purchasing gas at various points throughout the State, through wellhead purchases and transportation of gas through its own gathering systems.

Purchases of gas from Southern Union Gas Company, a wholly-owned gas company of Southern Union Company, operating in Northwest New Mexico and performing a swing function of being able to take gas production from the San Juan Basin, from the so-called jurisdictional or FPC-regulated gathering system and making those sales to the Gas Company of New Mexico when the market will not absorb those quantities of gas, namely in the summertime.

They sell those to El Paso, executed in 1973.

The Gathering Company assumed this function in 1953. At times when the Gas Company of New Mexico requires this gas supply for its New Mexico market to meet its winter peaks and higher load demands, that gas swings to Gas Company of New Mexico from the interstate market.

Q The Gathering Company is a separate corporation, though?

A Gathering Company is a separate Delaware corporation, authorized to do business in New Mexico.

Q And it's a wholly-owned subsidiary of Southern Union Company?

A Yes.

Q What is Southern Union Refining Company?

A Southern Union Refining Company is now a wholly-owned subsidiary of Southern Union Company and is also a Delaware corporation.

* * * * *

APPENDIX C

NATURAL GAS PRICES—SUMMARY

(Plaintiff's Exhibit 64)

	Estimate SUG[1] Purchases Leases In Suit	Estimate SUG[2] Purchases JAT Leases	New Mexico[3] Average Price	Intrastate Natural Gas Prices For Selected States[4] New Contracts	Renegotiated Or Amended	Average Price[5] All Jicarilla Gas	FPC Interstate Ceiling Price
1970	.1413	.1414	.1449				
1971	.1405	.1406	.1529			.148337	.1300
1972	.1374	.1389	.1884			.149210	.2358
1973	.1610	.1637	.2396			.183812	.2400
1974	.3279	.3260	.3201			.239484	.4360
1975	.3733	.3820	.4201	.5530-1.9824	.4524-1.8754	.312280	.5102
1976	.8933	.9200	.5801	1.0381-2.0260	.4000-1.9881	.350809	.5204
1977	1.6431	1.5658	.8243	.8857-2.1943	.7563-2.1244	.617022	.8958
						1.190179	

[1] Leases #10 (.50), 100, 101, 103, 104, 105, 106, 107, 145, 150, 153, 418 (.667).
[2] Leases #10 (.50), 38, 39, 76, 77, 100, 101, 102 (.417), 103, 104, 105, 106, 107, 109 (.077), 110 (.103), 121, 122, 124, 125, 145, 147, 150, 151, 153, 418 (.667), 420.
[3] New Mexico Oil and Gas Accounting Commission, Summaries by Year.
[4] *Monthly Energy Review*, Dept. of Energy, States Included: California, Kansas, Louisiana, Oklahoma, Texas.
[5] Based on data supplied by U.S.G.S.

Dr. Parker Report 3-30-79, #14

APPENDIX D

OPINION NO. 658

FEDERAL POWER COMMISSION
(10 C.A. App. Vol. VII, A-1250)

Before Commissioners: John N. Nassikas, Chairman
Albert B. Brooke, Jr., and Rush Moody, Jr.

Docket No. R-425

Area Rate for the Rocky Mountain Area)
)

OPINION NO. 658

OPINION AND ORDER ESTABLISHING JUST AND REASONABLE RATES AND INITIAL RATES IN THE ROCKY MOUNTAIN AREA

(Issued April 11, 1973)

* * *

[page 28]

We must take note also that producer bargaining in Rocky Mountain is less effective than elsewhere in the country and that the structure of the buyer segment could well have had a regressive impact upon exploration and development. El Paso is the sole interstate purchaser in the San Juan area, the Aneth subarea and in Apache County, Arizona; Montana-Dakota Utilities and Northern Natural are the sole purchasers in the Montana-Dakota subarea; only three transmission companies purchase in the Uinta-Green River subarea; and only two interstate pipelines purchase in the Colorado-Julesburg subarea.

We are not persuaded that time will correct the problem of the low rate levels prevalent in Rocky Mountain. From 1959 to 1969, average revenue for all deliveries of Rocky Mountain gas to interstate pipelines increased by only 1.2 cents from a level of 13.5 cents/Mcf to 14.7 cents. In contrast, since 1959, gas-well drilling costs have increased by 55 percent, wage levels in the oil and gas industry by 56 percent, and the general price level in the economy by 40 percent.

We note also that in the early 1950's, the contract prices in the San Juan area were roughly the same as for the Permian Basin. For the composite Rocky Mountain Area, the contract prices differed but little from the average prices for the Southwest market as a whole. The differential between prices in the Rocky Mountain Area and in other parts of the market widened thereafter. In the Southwest, gas prices increased through 1960 as the market became more competitive on the buying side. In the Rocky Mountain region, however, new contract prices have been virtually unchanged for a period of 20 years. Over this period, there have been sharp increases in price levels in the economy, in the value of gas as a commodity, in the costs of alternate fuels, and in the costs of doing business. . . .

APPENDIX E

AMENDMENT OF GAS PROCESSING AGREEMENT (10 C.A. App. Vol. VII, A-1219)

THIS AGREEMENT made and entered into this 1st day of December, 1971 by and between SOUTHERN UNION GAS COMPANY, a Delaware corporation (herein referred to as "Gas Company"), and SOUTHERN UNION PRODUCTION COMPANY, a Delaware corporation (herein referred to as "Production Company")

WITNESSETH THAT:

WHEREAS, Gas Company and Production Company entered into a Gas Processing Agreement dated so as to be effective as of January 1, 1971 respecting the processing of natural gas through the Lybrook Plant and the Huerfano Plant of Production Company (such agreement being herein called the "Processing Agreement"),

NOW, THEREFORE, Gas Company and Production Company do hereby mutually agree as follows:

1. Section 6 of Article I entitled "Definitions" of the Processing Agreement shall be and the same is hereby modified and amended so as to hereafter read and provide as follows:

> "Section 6. "Residue Volume" as used herein shall mean the Gathered Volumes of natural gas remaining after shrinkage arising out of (a) use of gas for processing plant fuel, (b) the plant processing of the gas for extraction of gasoline and other hydrocarbon constituents other than methane."

2. Section 2 of Article II entitled "Processing of Gas" of the Processing Agreement shall be and the same is

hereby modified and amended so as to hereafter read and provide as follows:

> "Section 2. The Gathered Volumes of gas that are gathered by Gas Company in the East Gathering System shall be processed by Production Company through the Lybrook Plant for extraction of gasoline and other hydrocarbon constituents other than methane; and likewise the Gathered Volumes of gas that are gathered by Gas Company in the West Gathering System shall be processed by Production Company through the Huerfano Plant for extraction therefrom of gasoline and such other hydrocarbon constituents other than methane as Production Company may elect from time to time. . . ."

APPENDIX F

GAS PROCESSING AGREEMENT DATED MAY 1, 1972 BETWEEN SOUTHERN UNION GAS COMPANY AND SOUTHERN UNION PRODUCTION COMPANY.

(10 C.A. App. Vol. VII, A-1221)

GAS PROCESSING AGREEMENT

THIS AGREEMENT made and entered into so as to be effective as of the 1st day of May, 1972, by and between SOUTHERN UNION GAS COMPANY, a Delaware corporation (herein referred to as "Gas Company"), and SOUTHERN UNION PRODUCTION COMPANY, a Delaware Corporation (herein referred to as "production Company"):

* * *

IV.

PAYMENT

Section 1. As consideration in addition to the benefits accruing to Gas Company from processing of gas delivered into its pipelines and as payment in full for all Plant Products removed from the Gathered Volumes and for gas used as fuel for plant operations and flared in connection with plant operations, Production Company shall pay to Gas Company the following amounts:

(a) Thirty-three and one-third percent (33-1/3% of the gross proceeds of sale of all Plant Products extracted from the Gathered Volumes and sold by Production Company that remain after deduction of any taxes based on the sale and any trucking or transportation charges

incurred by Production Company in the delivery of such products from the plants to the point of sale; plus

(b) An amount equal to that by which (i) the aggregate quantity of gas used by Production Company as fuel for operation of the Lybrook Plant and the Huerfano Plant, respectively, plus the quantity of gas that is flared by Production Company in operation of such plants determined in accordance with Section 1 of Article III hereof, plus the shrinkage in the Gathered Volumes of gas that is attributable to extraction of Plant Products therefrom determined in accordance with Section 2 of Article III hereof shall exceed (ii) 55 cubic feet of gas per gallon of Plant Products removed by Production Company from the Gathered Volumes, priced at the applicable General Service Rate Schedule of Gas Company on file and in effect from time to time with the New Mexico Public Service Commission covering sales of gas to industrial consumers on an interruptible basis.

Section 2. On or before the 15th day of each calendar month Production Company shall deliver to Gas Company a statement showing:

(a) The number of gallons of Plant Products extracted from the Gathered Volumes during the preceding month and the gross proceeds of sale therefrom after deduction of any taxes based on the sale and any trucking or transportation charges;

(b) The quantities of gas (i) that were used during the preceding month by Production Company as fuel for operation of the Lybrook Plant and the Huerfano Plant, respectively; (ii) that

were flared by Production Company in operation of such plants during the preceding month; (iii) that constitute shrinkage in Gathered Volumes attributable to extraction of Plant Products during the preceding month, and

(c) The amount due to Gas Company on account of plant processing during the preceding month.

Amounts due and owing to Gas Company because of processing during each calendar month shall be paid by Production Company to Gas Company on or before the 25th day of the next succeeding calendar month.

APPENDIX G

LETTER FROM HUBERT VELARDE, PRESIDENT, JICARILLA APACHE TRIBAL COUNCIL TO HONORABLE ROGERS C.B. MORTON DATED JUNE 29, 1973.

(10 C.A. App. Vol. I, A-20-22)

THE JICARILLA APACHE TRIBE

June 29, 1973

Honorable Rogers C.B. Morton
Secretary of the Interior
United States Department of Interior
Interior Building
18th and C Street Northwest
Washington, D. C. 20240

Re: Oil and Gas Leases, Jicarilla Apache Tribe

Sir:

Referring to our letter of March 23, 1973, with respect to royalty payments by the various lessees of the Jicarilla Apache Tribe under oil and gas mining leases, please be advised that our attorneys have been engaged in investigation of royalty payments made by various lessees for the past three months.

Our attorneys find a number of apparent violations of the provisions of these leases. Please address any correspondence with respect to these matters to Robert J. Nordhaus, attorney, 610 Simms Building, Albuquerque, New Mexico 87101, with a copy to the Jicarilla Apache Tribe.

1. Under provisions of paragraph 2(c), "Rental and Royalty" the lease provides that the "value" for the purpose of computing royalties shall be calculated on the basis of the highest price paid or offered—at the time of production

for the major portion of oil of the same gravity and gas and/or natural gasoline and/or all other hydrocarbon substances produced and sold from the fields where the leased lands are situated and the actual volume of the marketable product less content of foreign substances as determined by the Oil and Gas Supervisor. The actual amount realized by the lessee from the sale of said products may, at the discretion of the Secretary, be deemed evidence of or conclusive evidence of such value.

Royalties currently being paid for gas production on tribal lands are based on prices ranging from approximately 13¢ to over 30¢ for the same quality of gas produced. Further, the "value" for the purposes of the lease, should be based on the commodity value of gas, not a price artificially maintained at a low level by one or two purchasers of gas in a non-competitive market.

The Tribe demands that the Secretary take immediate action to determine the proper price basis for royalties paid to the Tribe and to secure an accounting from the companies for past royalties based on prices which do not reflect the "value" of the gas, as defined in the leases.

2. With respect to production under the majority of leases, no royalty is currently being paid on the value of natural gasoline and other hydrocarbon substances produced and saved from the leased land, contrary to the provisions of the leases.

3. As of March 31, 1973, Lessees owed past due amounts of over $400,000.00 for royalties, according to the audit reports of the accounting division of the U.S.G.S. in Roswell, New Mexico. In some cases these past due balances have been owing in lesser or greater amounts for 12 months or more. The attorneys for the Tribe are presently determining the status of past due balances. Demand is made that you require that these companies pay interest on past due balances, or that the penalty provisions of

Section 171.22 of the Regulations pertaining to leasing of tribal lands be invoked (25 CFR Sec. 171.22).

4. Section 3(c) of the leases in question provide that royalties shall be due and payable monthly on the last day of the calendar month following the calendar month in which produced. Uniformly over the period of production royalties have been paid sixty to ninety days after the end of the calendar month in which produced. Lessees should be required to pay estimated royalties in advance, or to pay interest on amounts past due under the provisions of the lease.

5. The monthly statements provided by the lessees under many leases currently do not show the value of by-products produced and saved, and no royalties are paid on such by-products. Reports currently show only gas and the price received from the producer.

Under paragraph 2(f) the lessees are required to exercise reasonable diligence in drilling and operating wells for oil and gas on the lands covered hereby while such products can be secured in paying quantities. It is believed that your department has failed to require diligence in drilling and developing the properties of the Tribe.

6. Under paragraph 4(b) the Tribe has the right to use sufficient gas free of charge for any buildings belonging to the Tribe by making connection at its own expense with well or wells thereon. Under this provision, your department should secure gas for school and other buildings belonging to the Tribe, at a cost that reflects only the cost of transporting the gas from the well head to tribal buildings.

7. It is the opinion of the Tribal Council of the Jicarilla Apache Tribe that as a result of various factors and influences, including price ceilings maintained by the Federal Power Commission, in which you have acquiesed, that royalties which have been paid to the Tribe over a period of

years have not been based upon the "value" of gas within the meaning of the above leases and that you have failed to protect the rights of the Tribe by securing for the Tribe royalties based on such "value". Your acquiescence in acceptance of royalties based on the prices maintained at an artificially low level as above stated has constituted a condemnation of the Tribe's property for public use without due process of law, with complete disregard for your obligation as guardian and trustee for the Tribe.

Demand is therefore made upon you for immediate action to correct the above mentioned discrepancies, or the Tribe will take action on its own behalf.

Yours very truly,

/s/ HUBERT VELARDE,
HUBERT VELARDE, President
Jicarilla Apache Tribal Council

APPENDIX H

MEMORANDUM TO SECRETARY OF THE INTERIOR FROM COMMISSIONER OF INDIAN AFFAIRS DATED JULY 29, 1974. (Plaintiff's Exhibit 29, No. 10)

United States Department of the Interior

BUREAU OF INDIAN AFFAIRS
WASHINGTON, D.C. 20245

Trust Services
Minerals

Memorandum
To: Secretary of the Interior Acting Deputy

From: Commissioner of Indian Affairs

Subject: Jicarilla Apache Tribe—Oil and Gas Royalty Issue

In letters dated March 23, 1973, and June 29, 1973, copies of which are enclosed, the Jicarilla Apache Tribe requested the Secretary to determine the true value of oil and gas produced on the Jicarilla Reservation since 1953 and take steps for collection of any delinquent royalties not paid, and further stated that if satisfaction of the request were not forthcoming the tribe would institute whatever legal action was deemed advisable. By letter dated June 25, 1973, from the Deputy Assistant Secretary to the President of the Jicarilla Apache Tribe, the Tribe's March 23 letter was acknowledged and by copy thereof, the Director, USGS, was requested to prepare a report on the matter. At this time, no report as requested has been received.

In a meeting in the Commissioner's office on June 25, the tribal representatives made a further request that the USGS, through the Secretary's Office, be asked to provide the tribe with the data previously requested, which would include the determination of:

1. The true value of the oil and gas produced on the Jicarilla Reservation from 1953 to present, which should be used in royalty computations.
2. The by-products and amounts thereof derived from the subject production. (These should be accounted for in the future.)
3. The cost of the manufacture of the above named by-products.
4. The value of the above by-products.

In compliance with the Tribe's wishes, we respectfully ask that you again request the Director, USGS, to provide the data previously indicated.

cc: Albuquerque Area Director, USGS

APPENDIX I

Attachment A to Appellant's Motion to Require Appellees to File Additional Bond or Other Security: (Filed July 10, 1986 in 10th Circuit Court of Appeals by Respondent herein)

ADDITIONAL ROYALTIES PAID BY SUPRON DEFENDANTS PURSUANT TO JUDGMENT

	Supron	Southland	Exxon	Knott	Hill	Total
Dec. 1979	$ 4,603.81	$ 3,780.41	$ 196.58	$ 49.39	-0-	$ 8,630.19
Jan. 1980	9,777.40	*	*	*	*	18,905.43
Feb. 1980	222.96	*	*	*	*	431.09
Mar. 1980	14,550.39	7,824.98	1,106.01	114.41		23,595.79
Apr. 1980	12,574.76	10,365.77	982.55	146.30		24,069.38
May 1980	15,143.94	10,640.60	561.67	130.46		26,476.67
June 1980	1,333.06	-0-	-0-	-0-		1,333.06
July 1980	-0-	-0-	-0-	-0-	-0-	-0-
Aug. 1980	6,694.45	5,520.99	110.39	94.89		12,420.72
Sept. 1980	4,163.22	2,647.38	-0-	33.35		6,843.95
Oct. 1980	7,695.86	6,329.77	263.67	101.16		14,390.46
Nov. 1980	19,856.55	15,713.77	1,682.38	190.85		37.443.55
Dec. 1980	2,462.53	1,987.83	-0-	7.77		4,458.13
Jan. 1981	6,118.87	4,927.80		120.86		11,167.53
Feb. 1981	5,102.02	4,232.99		90.93		9,425.94
Mar. 1981	5,788.59	4,646.19		97.99		10,532.77
Apr. 1981	7,457.87	6,130.60		113.11		13,701.58
May 1981	2,293.07	1,533.92		43.51		3,870.50
June 1981	1,327.62	755.83		13.58		2,097.03
July 1981	1,437.05	*	*	*	*	2,322.66
Aug. 1981	263.25	-0-		-0-		263.25
Sept. 1981	2,579.03	2,006.05		58.70		4,643.78
Oct. 1981	1,136.53	580.93		21.77		1,739.23
Nov. 1981	4,841.42	3,890.82		101.60		8,833.84
Dec. 1981	20,723.95	15,916.29		245.57		36,885.81
Jan. 1982	20,518.94	15,267.74		192.69		35,979.37
Feb. 1982	18,915.79	14,301.70		182.73		33,399.52
Mar. 1982	14,208.35	10,302.79		139.35	12.81	24,662.80
Apr. 1982	16,207.30	12,077.64		139.01	17.38	28,441.33
May 1982	3,081.38	884.43		36.12	.41	4,002.34
June 1982	*	*	*	*	*	16,259.79
July 1982						
Aug. 1982	13,678.35	10,264.04		84.04	30.31	24,056.74
Sept. 1982	22,649.49	-0-	-0-	-0-	-0-	22,649.49
Oct. 1982	*	*	*	*	*	26,890.01
Nov. 1982	27,737.27	-0-	-0-	-0-	-0-	27,737.27
Dec. 1982	32,912.39	-0-	-0-	-0-	-0-	32,912.39
Jan. 1983	39,232.61	-0-	-0-	-0-	-0-	39,232.61
Feb. 1983	*	*	*	*	*	26,034.63
March 1983	13,358.27	9,439.15	-0-	-0-	-0-	22,797.42
March 1983	416.385	8.575	-0-	-0-	-0-	424.96
April 1983	19,513.41	15,302.105	-0-	213.455	108.33	35,137.30
May 1983	*	*	*	*	*	15,345.62
June 1983	*	*	*	*	*	8,835.52
July 1983	*	*	*	*	*	9,302.96
Aug. 1983	*	*	*	*	*	12,444.30
Sept. 1983	*	*	*	*	*	15,566.30
Nov. 1983	*	*	*	*	*	20,382.78
GRAND TOTAL						$766,977.79

Attachment A

APPENDIX J
(10 C.A. App. Vol. VII, A-1297-1301)

IN THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF NEW MEXICO

THE JICARILLA APACHE TRIBE,
Plaintiff,

v. No. ___ Civil

SOUTHERN UNION GAS COMPANY,
a Delaware corporation, *et al.*,
Defendants.

STIPULATION FOR SETTLEMENT

Come now the Plaintiff, The Jicarilla Apache Tribe, an Indian Tribe organized and incorporated under the laws of the United States of America, (the "Tribe"), Defendant Gas Company of New Mexico, a division of Southern Union Gas Company, a Delaware corporation, (formerly Southern Union Gas Company), ("GCNM"), and Defendant Southern Union Gathering Company and hereby stipulate and agree as follows:

1. The Tribe and GCNM have entered into a Settlement Agreement, a Royalty Gas Gathering Agreement and a Royalty Gas Purchase Contract, all of even date herewith settling other matters in dispute between the Tribe and GCNM, which Agreements are incorporated herein by reference.

2. The Jicarilla Apache Tribal oil and gas leases covering Tribal lands in Rio Arriba County, New Mexico, give the

Tribe the right to take its royalty gas in kind upon the giving of notice as provided for therein. It is agreed with respect to all of the tribal oil and gas leases on Tribal lands that if and to the extent the Tribe takes its royalty gas in kind, and if and to the extent GCNM may at such time have gathering systems connected to such wells, then subject to the payment of reasonable transportation charges therefor, GCNM agrees to gather and deliver, and to permit the Tribe to take its share of the royalty gas from wells from which GCNM purchases gas at a point on the Tribal reservation lands from the GCNM gathering pipeline system, upon reasonable written notice, which shall be not less than ninety (90) days, from the Tribe to GCNM, any necessary tap, connections and other facilities necessary to effect such delivery shall be installed by GCNM at GCNM's expense, and the Tribe shall provide rights-of-way and other surface rights therefor free of cost to GCNM. The point of delivery to the Tribe shall be at a point on GCNM's existing gathering system having the pipeline capacity to deliver such royalty gas without construction of any additional pipeline or compression facilities.

3. GCNM's performance under the Royalty Gas Gathering Agreement with the Tribe is excused until it is established by a court of competent jurisdiction or by agreement of the parties hereto and the parties claiming otherwise that GCNM has the right to gather and deliver the Tribe's royalty gas taken in kind. Until such determination has been made, GCNM's performance under said agreement is subject to the claims of Southern Union Production Company and other parties having contractual rights to process said gas or to the liquid products derived therefrom. In the event GCNM, Southern Union Company, or any other subsidiary or division of Southern Union Company does not acquire ownership of the Lybrook Processing Plant, and/or successfully negotiate contractual arrangements to permit GCNM to gather and deliver the

Tribe's royalty gas taken in kind and to permit the Tribe to process such gas at the point of such delivery, by March 1, 1977, the parties hereto agree to resume negotiations to arrange an alternate method of delivery of the Tribe's royalty gas. GCNM further agrees to purchase, and the Tribe agrees to sell to GCNM, under the terms of the Gas Purchase Contract of even date herewith, any portion of the Tribe's royalty gas taken in kind which is in excess of the Tribe's daily requirements.

4. If the Tribe does not elect to take its natural gas in kind, but a producer selling under a contract to GCNM is ordered by the Court or voluntarily agrees to make accounting to the Tribe for its royalty interest on the basis of a net realization method, other liquids method or BTU adjustment method of accounting, then GCNM agrees to cooperate with said producer in furnishing information for such accounting to the Tribe.

5. GCNM shall pay the Tribe within ten (10) days after the approval of this stipulation by the Court and entry of the same as its judgment, the sum of Six Hundred Thousand Dollars ($600,000.00) for settlement of all claims made by the Tribe against GCNM and Southern Union Gathering Company in this case and for execution concurrently herewith of an agreement concerning pipeline rights-of-way, facility sites and other surface leases or easements and for agreement that all claims and causes of action of the Tribe against GCNM and Southern Union Gathering Company set forth and alleged in the First Amended Complaint on file herewith are released and discharged and all such claims and causes of action are dismissed with prejudice as to the defendants GCNM and Southern Union Gathering Company.

6. GCNM's agreement to gather and deliver the Tribe's royalty gas may be subject to regulations by State or Federal authorities having jurisdiction. To the extent that such State or Federal authorities have jurisdiction, the parties agree that this agreement is subject to such rules

and regulations as may be imposed by such authorities. The parties agree to cooperate in seeking any approvals which may be required by such authorities, if any, and to secure the agreement provided for in Paragraph 3 above, to effectuate the intent of this agreement.

7. This Stipulation shall be construed to pertain to all claims of the Tribe against GCNM and Southern Union Gathering Company relating to oil and gas, including rights-of-way matters, accruing to the date of this Stipulation. All of said claims merge into this Stipulation and are governed by its terms.

8. All matters in controversy in this case between the Tribe and the Defendants GCNM and Southern Union Gathering Company having been settled, the parties hereto request the Court to enter this Stipulation as its Final Judgment in this case, and the case shall be dismissed with prejudice in its entirety as to GCNM and Southern Union Gathering Company, each party to bear its own costs.

Executed this 21st day of October, 1976, in several counterparts, each of which shall be considered an original.

THE JICARILLA APACHE TRIBE

ATTEST:

/s/ Barbara Gonzales
Secretary

By /s/ Dale Vigil
Acting President

NORDHAUS, MOSES & DUNN

By /s/ ROBERT J. NORDHAUS
Robert J. Nordhaus
Attorneys for
The Jicarilla Apache Tribe

GAS COMPANY OF NEW MEXICO

ATTEST:

/s/ Illegible
Secretary

By /s/ W. T. Baumhouse
President

MONTGOMERY, FEDERICI,
ANDREWS & HANNAHS

/s/ JACK HERTZ
Jack Hertz
Vice President and General
Attorney for Gas Company of
New Mexico

By /s/ William Federici
Counsel for Gas Company of
New Mexico

SOUTHERN UNION
GATHERING COMPANY

ATTEST:

/s/ Illegible
Secretary

By /s/ Illegible
Vice President

MONTGOMERY, FEDERICI,
ANDREWS & HANNAHS

By /s/ William Federici
Counsel for Southern Union
Gathering Company

APPENDIX K

42 FEDERAL REGISTER 40263, AUGUST 9, 1977

Geological Survey

[NTL-5]

VALUE OF NATURAL GAS FOR ROYALTY PURPOSES

On May 4, 1977, the Geological Survey published in the FEDERAL REGISTER (Vol. 42, No. 86, pp. 22610-22611) its final notice to Lessees and Operators, NTL-5. This Notice sets forth the procedures to be utilized for royalty computation purposes in determining the value of natural gas produced from Federal and Indian oil and gas leases under the jurisdiction of the Geological Survey.

Pursuant to a request by the Acting Deputy Commissioner of Indian Affairs, the application of NTL-5 to oil and gas leases on the Jicarilla Apache Indian Reservation in New Mexico is hereby suspended for an indefinite period, effective as of 7 a.m., June 1, 1977.

V.E. McKELVEY,
Director.

(1) (1) (8) (7)

Nos. 86-219, 86-224, 86-225 and 86-226

Supreme Court, U.S.
FILED
OCT 24 1986
JOSEPH F. SPANIOL, JR.
CLERK

In the Supreme Court of the United States

OCTOBER TERM, 1986

SOUTHERN UNION COMPANY, PETITIONER

v.

JICARILLA APACHE TRIBE, ET AL.

SOUTHLAND ROYALTY COMPANY, PETITIONER

v.

JICARILLA APACHE TRIBE, ET AL.

EXXON CORPORATION, PETITIONER

v.

JICARILLA APACHE TRIBE, ET AL.

UNICON PRODUCING COMPANY, PETITIONER

v.

JICARILLA APACHE TRIBE, ET AL.

ON PETITIONS FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

BRIEF FOR THE SECRETARY OF THE INTERIOR IN OPPOSITION

CHARLES FRIED
Solicitor General

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Department of Justice
Washington, D.C. 20530
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15 pp

QUESTION PRESENTED

Whether the court of appeals correctly held that petitioners, which produce natural gas on the Jicarilla Apache Reservation under lease agreements with the Tribe, are obligated to pay the Tribe royalties under a "dual accounting" method.

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In the Supreme Court of the United States

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SOUTHERN UNION COMPANY, PETITIONER

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ON PETITIONS FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

BRIEF FOR THE SECRETARY OF THE INTERIOR IN OPPOSITION

OPINIONS BELOW

The opinion of the en banc court of appeals (Pet. App. 1a-14a)[1] is reported at 782 F.2d 855, and the supplemental opinion of the en banc court (Pet. App. 18a-19a) is re-

[1] "Pet. App." refers to the joint petition appendix filed in No. 86-219.

ported at 793 F.2d 1171. The opinion of the three-judge panel of the court of appeals (Pet. App. 21a-65a) is reported at 728 F.2d 1555. The district court's opinion (Pet. App. 104a-137a) is reported at 479 F. Supp. 536.

JURISDICTION

The judgment of the court of appeals was entered on January 23, 1986 and petitions for rehearing were denied on April 15, 1986 (Pet. App. 15a-16a). Justice White extended the time for filing the petitions for a writ of certiorari to August 13, 1986 and the petitions were filed on that date. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

The Jicarilla Apache Tribe occupies a 742,315 acre Executive Order reservation in northwestern New Mexico. Since the early 1950's, the Tribe has leased reservation land for oil and gas production. The leases, which have been approved by the Secretary of the Interior, are governed by the provisions of a standard lease form entered into pursuant to federal statutes and regulations. See Indian Mineral Leasing Act (IMLA), 25 U.S.C. 396a-396g; 25 C.F.R. Pt. 211.[2]

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[2] The IMLA was enacted in 1938 to provide a uniform statutory scheme for Indian tribes to lease unallotted lands for mining purposes. See S. Rep. 985, 75th Cong., 1st Sess. 3 (1937); see generally *Montana* v. *Blackfeet Tribe of Indians*, No. 83-2161 (June 3, 1985). The statute provides that unallotted lands within Indian reservations may, with the approval of the Secretary, be leased for mining purposes, by authority of the authorized spokesmen for the Tribe (25 U.S.C. 396a). The statute also provides that lessee operations affecting restricted Indian lands shall be subject to rules and regulations promulgated by the Secretary (25 U.S.C. 396d). See 25 C.F.R. Pt. 211. Those regulations are incorporated in the lease agreements here. See Pet. App. 382a.

In May 1975, the Tribe brought suit against petitioners, contending that their conduct breached the lease agreements and violated the antitrust laws. Of particular relevance here, the Tribe claimed that petitioners had failed to develop their leases diligently, had failed to drill offset wells to protect the leases from drainage, and had failed to account properly for royalties. The Tribe specifically argued that the leases required petitioners to pay royalties based on a "dual accounting" method.[3] The Tribe later named the Secretary of the Interior as a defendant, claiming that the Secretary had failed to ensure that petitioners performed their lease obligations and had thereby breached fiduciary duties owed to the Tribe. Pet. App. 104a-105a, 108a-109a, 117a.

The district court rejected the Tribe's claims that petitioners had failed to develop the leases (Pet. App. 120a) and protect against drainage (*id.* at 124a), but concluded that the Secretary should have engaged in more rigorous monitoring of the lessees' activities to ensure diligent development and drainage protection (*ibid.*). Turning to the Tribe's challenge to petitioners' accounting method, the court stated that "where, as here, gas produced from

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[3] The leases provide that royalties shall be paid as a percentage of the "value" of the gas produced. See Pet. App. 379a. Industry practices provide a number of accounting methods for determining value, including the "BTU adjustment" method and the "net realization" method. Under the BTU adjustment method, value is determined on the basis of the wellhead sales price of the unprocessed natural gas, adjusted to reflect the heating value of the gas. Under the net realization method, value is determined on the basis of the sales price of the individual components of the natural gas, adjusted to reflect the costs of separating and processing those components. Under "dual accounting," the lessee accounts for the value of the natural gas using both accounting methods and then calculates and pays royalties based on the higher of the two values. Prior to the sharp increase in oil prices in the 1970's, the BTU adjustment method, then used by petitioners without objection from the Secretary, provided the higher royalties.

the lease is processed into component products, dual accounting is required by the terms of the lease. Accordingly, the Secretary had the obligation to require [petitioners] to account on the net realization method" (*id.* at 131a). The district court ordered the Secretary to require the petitioners to render an accounting by the "dual accounting method for the years 1970 to the present" (*id.* at 135a) and to submit the accounting to the district court for its approval. The district court ultimately ordered petitioners to pay the Tribe $343,738.81 in royalties.

On appeal, petitioners challenged the district court's determination that the Tribe was entitled to receive royalties under the dual accounting method. The Secretary urged that he had not violated fiduciary duties owed to the Tribe but did not challenge the district court's determination that dual accounting is required. The Tribe challenged other aspects of the district court's ruling.

The court of appeals panel reversed the district court's determination that the Tribe is entitled to dual accounting. The court stated that "[f]rom 1950 to 1979 without exception, and without variation, the Secretary and the USGS [United States Geological Survey] had construed the lease provisions and [Interior's leasing] regulations to require dual accounting not by all lessees, but *only* in instances where the lessee owned the processing plant (or received added money for its products)" (Pet. App. 24a (emphasis in original)). The court concluded that "[t]he original construction placed on the lease and regulations by the Secretary as to this issue must be applied to and through the conclusion of these proceedings" (*id.* at 29a). The court found "no basis for the trial court's determination as to fiduciary standards" and declined to decide "whether or not the Secretary owes the tribe a fiduciary duty as to the matters under consideration" (*id.* at 30a).

Judge Seymour dissented, concluding that dual accounting should be required. She noted that the Secretary now agreed with the district court that dual accounting should be used (Pet. App. 42a-43a). Concluding that the Secretary owes fiduciary duties to the Tribe, she stated "the true issue in this case is not whether the Secretary's earlier application of the royalty terms was reasonable; rather, it is whether the alternative interpretation requiring dual accounting is also reasonable *and* better promotes the Tribe's interest" (*id.* at 45a (emphasis in original)). She concluded that either interpretation of the lease and Interior regulations, requiring or not requiring dual accounting, would be reasonable, and that the Secretary's choice between these interpretations should be based on the alternative that provides the greatest benefits to the Tribe (*id.* at 48a).

The Tribe petitioned for rehearing en banc. The court of appeals granted the petition and reversed the panel decision, adopting Judge Seymour's dissent with minor modifications not relevant here (Pet. App. 3a-4a). The Secretary then moved for modification of the court's decision to delete that part of the opinion (*id.* at 41a-48a) discussing fiduciary duties, arguing that, because the Secretary had agreed to require dual accounting, the issue was moot. The court denied the motion (*id.* at 18a). However, the court, on its own motion, supplemented its en banc opinion to make clear that petitioners are liable for past nonpayment of royalties under the dual accounting method (*id.* at 18a-19a). The court stated (*id.* at 19a (footnote omitted)):

> While the Secretary failed in its duty to represent the Tribe's interests in the present case, the relationship between the Tribe and [petitioners] is contractual. The failure of the Secretary to require dual accounting resulted in the lessees paying an insufficient amount of royalties under the contract. That the Secretary breached [his] fiduciary duty to properly en-

force the leases does not excuse the lessees from subsequently having to pay the amounts determined to be owed under the leases. *Cf. Atlantic Richfield Co. v. Hickel*, 432 F.2d 587, 592 (10th Cir. 1970).

ARGUMENT

The court of appeals reasonably concluded that petitioners are obligated under their lease agreements to pay royalties on a dual accounting basis. That determination is consistent with the Secretary's present interpretation of the particular lease agreements at issue here, and it does not conflict with any decision of this Court or of other courts of appeals. The court incorrectly found that the Secretary, in the past, had breached fiduciary duties to the Tribe. However, the Tribe and the Secretary now agree on the proper method of calculating royalties in this case, and those royalties remain subject to collection under the lease agreements. Under these circumstances, the court's finding that the Secretary breached fiduciary duties has little remaining practical importance. Accordingly, this case does not warrant this Court's review.

1. Petitioners characterize this case as presenting important questions concerning the United States' fiduciary duties to the Nation's Indian tribes. However, this case, in its current posture, presents what is essentially a narrow contractual dispute between petitioners and the Jicarilla Apache Tribe. The court of appeals did discuss the Secretary's fiduciary duties to that Tribe, employing an analysis that we consider largely mistaken.[4] But whether or not that analysis is correct, it has only limited relevance

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[4] Assuming that the IMLA creates fiduciary obligations, we submit that the Secretary's conduct in these cases meets the "ordinarily prudent man" standard that the Claims Court has applied in Indian trust cases. See, *e.g., Navajo Tribe of Indians* v. *United States*, 9 Cl. Ct. 336, 400 (1986). Prior to the dramatic increase of oil and gas prices in

at this juncture. The Secretary presently agrees, quite apart from any fiduciary obligations that might exist, that dual accounting should be utilized in this case. There is no substantial difference between the position of the Secretary and the Tribe at this time and there is little to be gained from examining the question of fiduciary obligations in an abstract context at petitioners' behest, particularly when neither the Secretary nor the Tribe desires further review of this question.[5]

The focus of the present dispute is *petitioners'* obligations to the Tribe. The court of appeals correctly observed that "the relationship between the Tribe and [petitioners] is contractual (Pet. App. 19a), an observation with which all parties, including the Secretary, the Tribe (Br. in Opp. 24-25), and petitioners (86-219 Pet. 20; 86-226 Pet. 12, 14), agree. As the Tribe explains, petitioners "agreed to lease provisions reasonably susceptible to the interpretation that royalties be based on the highest value reasonably obtainable under their [leases]" (Br. in Opp. 24-25). The Tribe brought suit against petitioners, successfully urged its interpretation of the lease agreements' royalty provisions before the district court, and ultimately prevailed before the court of appeals.[6]

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the early 1970's, the BTU adjustment method for calculating gas value generally produced higher royalties than the net realization method. Furthermore, prior to the district court's decision, the Secretary maintained legitimate reservations whether the lease terms permitted dual accounting. Finally, it is not clear that requiring dual accounting, in every case, will be in the best long-term interest of the Tribe.

[5] There will, of course, be ample opportunity in future cases to examine the Tenth Circuit's interpretation of the United States' trust responsibilities to the Indian tribes. See, *e.g.*, *United States* v. *Cherokee Nation of Oklahoma*, cert. granted, No. 85-1940 (Oct. 6, 1986).

[6] Under the lease, the Tribe has the authority "that any lessor has under an oil and gas lease to enforce its terms and conditions and to so manage the property" (Pet. App. 7a). The Secretary clearly plays an

In our view, the meaning of the leases' royalty terms is open to legitimate debate. But we believe that they can be plausibly interpreted to require dual accounting and, at least in the present circumstances, we endorse that interpretation. The court of appeals' explanation (Pet. App. 45a-48a) is consistent with the language of the lease agreements. There is no conflict among the circuits concerning interpretation of the language at issue, and the court of appeals' interpretation may not be controlling in other Indian lease agreements executed under different circumstances. Thus, this contractual dispute does not warrant this Court's review.

2. Petitioners further argue that, despite their contractual obligations to the Tribe, the United States, rather than they, should pay any past royalties owed to the Tribe. Petitioners characterize themselves as "innocent" third parties (86-219 Pet. 16; 86-224 Pet. 28; 86-226 Pet. 25; see 86-225 Pet. 27) who have been forced to account for the Secretary's errors. This argument is plainly insubstantial.

Petitioners are sophisticated oil and gas producing companies that sought out leases from the Jicarilla Apache Tribe and agreed to open-ended leasing terms, accepting an element of commercial uncertainty in the pursuit of their economic self-interest. As we have already noted,

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important role in formulating lease terms and enforcing the lease agreements. However, as petitioners concede, "the Indians retain a significant role in making and supervising such leases" (86-225 Pet. 7). This Court has stated that "[w]hile the United States has exercised its supervisory authority over oil and gas leases in considerable detail, we find nothing in this regulatory scheme which would preclude [Indian lessors] from seeking judicial relief for an alleged violation of the lease." *Poafpybitty* v. *Skelly Oil Co.*, 390 U.S. 365, 373 (1968). Indeed, "there is nothing in the lease or regulations requiring the Indians to seek administrative action from the Government instead of instituting legal proceedings on their own" (*ibid.*). Accordingly, the litigation, as between the Tribe and petitioners, is no more than an action in contract to remedy violations of the lease terms.

those agreements can plausibly be read to require dual accounting. Furthermore, the agreements expressly leave the methodology for determining value, in part, to the Secretary's discretion.[7] And it is obviously petitioners, rather than the Secretary, who have enjoyed the quid pro quo for which additional royalty payments are due under the leases.

Nor is there otherwise any unfairness or impropriety in requiring petitioners to pay past royalties. As petitioners fully understand, their monthly submission of royalties and accompanying information is subject to correction after the Secretary's representative[8] has had an opportunity to make an independent audit. *Supron Energy*

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[7] Section 3(c) of the standard lease agreement provides (Pet. App. 379a-381a (emphasis added)):

> During the period of supervision, "value" for the purposes hereof may, in the discretion of the Secretary, be calculated on the basis of the highest price paid or offered * * * at the time of production for the major portion of the oil of the same gravity, and gas, and/or natural gasoline, and/or all other hydrocarbon substances produced and sold from the field where the leased lands are situated, and the actual volume of the marketable product less the content of foreign substances as determined by the oil and gas supervisor. The actual amount realized by the lessee from the sale of said products may, in the discretion of the Secretary, be deemed mere evidence of or conclusive evidence of such value. * * * *It is understood that in determining the value for royalty purposes of products * * * that are derived from treatment of gas, a reasonable allowance for the cost of manufacture shall be made, * * * and that royalty will be computed on the value of gas or casing-head gas, or on the products thereof * * *, whichever is the greater.*

Section 3(c) reflects Interior's present regulations governing determination of value. See 25 C.F.R. 211.13.

[8] Prior to 1983, the United States Geological Survey (USGS) was responsible for managing all federal and Indian oil and gas leases. The Minerals Management Service has succeeded the USGS as the responsible agency. See 25 C.F.R. Pts. 211, 212; 30 C.F.R. 206.100.

Corp., 46 I.B.L.A. 181, 189 (1980) (the Secretary bills lessees for royalties "on the basis of the information contained in monthly reports which they submitted, *subject to post audit*" (emphasis in original; reproduced at Pet. App. 187a)). Where, as here, lessees submitted royalty payments in a particular manner later found by the Secretary or a court to be inconsistent with the terms of the leases and regulations, the Secretary may demand payment of the deficiency. See *Atlantic Richfield Co.* v. *Hickel*, 432 F.2d 587, 591 (10th Cir. 1970); see also *Foote Mineral Co.*, 85 Interior Dec. 171, 181 (1978) ("the Government is not estopped from demanding royalty payments owed by lessees, even if it has accepted improper royalty payments in the past"), rev'd on other grounds, 654 F.2d 81 (Ct. Cl. 1981). Indeed, Congress, through the Federal Oil and Gas Royalty Management Act of 1982, 30 U.S.C. 1701 *et seq.*, has recognized that lease accounts are subject to correction and has directed the Secretary to "audit and reconcile, to the extent practicable, all current and past lease accounts for leases of oil or gas and take appropriate actions to make additional collections or refunds as warranted" (30 U.S.C. 1711(c)(1)).[9]

In sum, the court of appeals' requirement that petitioners pay past royalties simply enforces petitioners' contractual obligations to the Tribe and does not merit this Court's review.

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[9] Congress has further instructed the Secretary to "aggressively carry out his trust responsibility in the administration of Indian oil and gas" (30 U.S.C. 1701(a)(4)), to "give priority to auditing those lease accounts identified by a State or Indian tribe as having significant potential for underpayment" (30 U.S.C. 1711(c)(1)) and to seek payment of interest on any underpayments from prior periods (30 U.S.C. 1721(a)).

CONCLUSION

The petition for a writ of certiorari should be denied.
Respectfully submitted.

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SOUTHERN UNION COMPANY,
UNICON PRODUCING COMPANY,
SOUTHLAND ROYALTY COMPANY and
EXXON CORPORATION,
Petitioners,

v.

JICARILLA APACHE TRIBE,
DONALD P. HODEL, Secretary of the
United States Department of the Interior
and STATE OF NEW MEXICO,
Respondents.

On Petitions for a Writ of Certiorari to the United States Court of Appeals for the Tenth Circuit

PETITIONERS' JOINT REPLY BRIEF

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PETITIONERS' JOINT REPLY BRIEF

Petitioners Southern Union Company, Unicon Producing Company, Southland Royalty Company, and Exxon Corporation submit this joint reply to the briefs in opposition filed by the Jicarilla Apache Tribe and the Secretary of the Interior. Respondents have failed to offer any substantial arguments against review by this Court.

On the contrary, in their efforts to divert attention away from the actual ruling of the court below, they have only underlined the important issues raised by these petitions.

1. We note, first of all, that respondents do little or nothing to rebut our basic critique of the Tenth Circuit's analysis of fiduciary duty. The Secretary, in fact, acknowledges that the Tenth Circuit's analysis is "largely mistaken." Opp. at 6. He endorses the Claims Court's "ordinary prudent man" standard for review of his actions in a fiduciary capacity, Opp. at 6 n.4—thus impliedly rejecting the Tenth Circuit's requirement that he resolve every ambiguity, and make every discretionary choice, in the way that best serves the immediate interests of the Tribe. More specifically, he makes it clear that his failure to impose dual accounting on these petitioners from 1950 to 1979 was not, in his view, a breach of fiduciary duty. *Ibid.* Indeed, he states that prior to the decision in this case, he had doubts about whether dual accounting was even *permitted* under the leases, and adds that even now he does not believe that dual accounting always serves the long-term interest of the affected Indians. *Ibid.*

As for the Tribe, it makes only a perfunctory effort to defend the Tenth Circuit's analysis. It cites two cases for the proposition that the Secretary, as a fiduciary, is dutybound to impose dual accounting because that royalty system may enhance tribal revenues. But neither case supports the Tribe's suggestion that the Secretary has no discretion and must maximize short-term royalty income to the Tribe.[1]

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[1] The first cited case—*Kenai Oil & Gas, Inc. v. Department of Interior*, 671 F.2d 383, 386 (10th Cir. 1982)—does state in *dictum* that the Secretary has a duty to maximize Indian lease revenues. However, the Tenth Circuit there emphasized the Secretary's "broad discretion" to consider all relevant factors affecting Indian interests, not just their immediate profit. *Id.* at 387. Moreover, it stated that any exercise of the Secretary's discretion is reviewable only under the usual administrative-law standard—*i.e.*, whether it was

2. In lieu of defending the ruling below, both respondents rely, in large part, on the fact that the Secretary has departed from the policy that prevailed from 1950 to 1979 and is now endorsing the use of dual accounting under these leases. The Tribe seeks to portray this case as a fight between the Secretary and petitioners, with petitioners cast in the role of challengers to the Secretary's own independent interpretation of the leases or independent policy choice under those leases. The Secretary's approach, by contrast, sounds more like a variant of a mootness argument. He is unwilling to articulate a general policy favoring dual accounting and seek deference to that policy. Instead, he simply states that, regardless of any ruling by this Court, he intends to mandate dual accounting *on these particular leases*, and suggests that this fact argues against review of the decision below.

The problems with these arguments are apparent. First, of course, even assuming that the Secretary would continue to require dual accounting after a reversal, that fact hardly justifies leaving in place a ruling that mandates this particular royalty system *permanently* as well as *retroactively*. It is one thing to give deference to the Secretary's current interpretation of the leases or his current exercise of his discretion. It is quite another to extend that current judgment, not only to an indefinite future, but also to a previous period when a different Secretary was taking a very different view.

Second, regardless of the present policy preferences of the Secretary with respect to these leases, a denial of

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"arbitrary, capricious, an abuse of discretion, or contrary to law." *Id.* at 386.

The other decision cited by the Tribe, *Marathon Oil Co. v. United States*, 794 F.2d 1461 (9th Cir. 1986), is even less apposite. In that case, the Secretary *voluntarily* initiated a change in the royalty formula under a federal mineral lease, and that decision was upheld against a challenge by an oil company using the usual "arbitrary and capricious" standard. The obligations of the Secretary as a fiduciary were not at issue, since the case did not involve rights of Indians.

review here would leave in place a decision that fundamentally alters prevailing assumptions about judicial review of secretarial actions affecting Indian tribes. The Tenth Circuit's reasoning would be equally applicable to several thousand identical leases on other Indian lands.[2] And it could control the interpretation and administration of many other commercial arrangements supervised by the Secretary for Indians.[3] In all of these areas, the Secretary henceforth would have only one permissible choice—resolving every ambiguity and making every choice in the manner that maximizes short-term tribal revenue. If this far-reaching decision is wrong, as we and the Government both believe, then the fact that the Secretary fortuitously approves of the particular royalty system mandated by that decision for these leases does not lessen the need for review.

Finally, the factual predicate of respondents' arguments—the suggestion that the Secretary has made a considered policy judgment in favor of dual accounting under these leases—is itself subject to serious question. In reality, the Secretary never took any action to require dual accounting by Jicarilla lessees—other than those that also owned the gas processing plant—until he was ordered to impose this system by the district court *in this case* in 1979.[4] Moreover, since that time there is no

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[2] The Secretary suggests that the "court of appeals' interpretation may not be controlling in other Indian lease agreements executed under different circumstances." Opp. at 8. But this assurance is insupportable since (1) all Indian oil and gas leases have involved the same basic form agreement for more than four decades, and (2) the Tenth Circuit relied on no circumstances that are peculiar to the Jicarilla context.

[3] The Tenth Circuit's use of a "stricter standard" of review in a fiduciary context has already been noted, although not accepted or relied on, by the Ninth Circuit in *Assinboine and Sioux Tribes v. Board of Oil and Gas Conservation*, 792 F.2d 782, 792 n.9 (1986).

[4] See J.A. 12a (dissenting opinion of Seth, J.). Indeed, the Secretary himself indicates the importance of this linkage, when he notes that "prior to the district court's decision, [he] maintained

indication that the Secretary has ever voluntarily extended this rule to any of the thousands of identical leases in effect on other Indian and public lands.[5] These facts are reflected in the Secretary's careful comments that the decision below is "consistent with [his] *present* interpretation of the *particular* lease agreements at issue *here*," Opp. at 6 (emphasis added), and that he endorses the requirement of dual accounting "at least in the present circumstances," Opp. at 8. In the absence of some explanation differentiating these sixteen leases from thousands of others concededly containing identical provisions, it seems clear that this endorsement is more a reflection of litigation strategy than a factor that should influence the Court's decision on the pending petitions for review.

3. The other argument against review raised by the Secretary is the suggestion that this is really just a "narrow contractual dispute between petitioners and the Jicarilla Apache Tribe." Opp. at 6. As the premise for this argument, the Secretary describes the Tenth Circuit as ruling "that petitioners are obligated *under their lease agreements* to pay royalties on a dual accounting basis." *Ibid.* (emphasis added). This description, in turn, becomes the sole basis of the Secretary's additional contention that it is appropriate to impose the burden of retroactive liability on petitioners rather than the Government. As he puts it, retroactive payments by lessees are clearly appropriate "[w]here, as here, lessees submitted royalty payments in a particular manner later found by the Secretary or a court to be *inconsistent with the terms of the leases and regulations*." Opp. at 10 (emphasis added).

The problem with this entire line of argument is its reliance on a flat mischaracterization of the Tenth Cir-

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legitimate reservations about whether the lease terms permitted dual accounting." Opp. at 6 n.4.

[5] As Judge Seth put it last January, these apparently are the "*only* Indian or public land leases in the country where this construction is now applied." J.A. 12a (emphasis in original).

cuit's decision. As the Secretary implicitly concedes, a finding of breach by the lessees here would depend upon a prior finding that the lease terms require dual accounting. But far from making such a finding, the Tenth Circuit acknowledged that a contrary interpretation was "reasonable," J.A. 48a, and it relied for its holding solely on the theory that the Secretary has an obligation to interpret and apply *ambiguous* language in the manner that best promotes the Tribe's interests.[6] J.A. 45a. The real "breach" here, in the court's view, was not a violation of the lease terms by petitioners but a breach by the Secretary of his supposed fiduciary duty to maximize Indian royalty payments to the extent possible within the limits left open to him by the leases and regulations themselves.[7]

Once this clarification is made, it becomes clear that the decision below does not involve a "narrow contractual dispute" at all; it is a broad and novel analysis of the duties imposed on the Secretary *qua* fiduciary, which has serious implications with respect to the rights and expectations of all private parties who contract with Indians under governmental supervision. It also becomes clear that the imposition of retroactive liability on petitioners is indefensible.[8] Even assuming that the Tenth

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[6] Even the Tribe itself acknowledges that the leases and regulations "vest discretion in the Secretary" to choose from among various royalty systems. Opp. at 9. *See* Lease ¶ 3(c), J.A. 380a (price received by lessee may be taken as "conclusive evidence" of value).

[7] The suggestion that petitioners violated the terms of the leases by not engaging in dual accounting is also inconsistent with the Secretary's argument that his previous administration of these leases comported with his fiduciary duties. *See* Opp. at 6 n.4. If, in fact, a requirement of dual accounting could be discerned at this late date in the lease terms themselves, the Secretary would have breached his obligations by failing to notice this requirement for almost thirty years. And he would still be breaching his duty by failing to require dual accounting under many other identical leases.

[8] By shifting the focus of his discussion to a supposed breach of the lease terms by petitioners, the Secretary neatly avoids any

Circuit's fiduciary theories were correct, they would not begin to show how petitioners have in any way breached *their* duties under the leases. They, after all, simply followed the royalty system approved by the Secretary at the time they were making these past royalty payments. And that is all that the leases can fairly be read to require of them.

4. In view of the strained nature of the Secretary's arguments, it seems reasonable to take a closer look at the factors that might lead him to counsel against review of a seminal decision with which he flatly disagrees. We have already alluded to one such factor—the identity of the parties who have been ordered to pay damages here to recompense the Tribe for the Secretary's breach of fiduciary duty. The Government's concerns about the Tenth Circuit's analysis are likely to be much more forcefully expressed in a later case where, as is usually true, the Secretary as fiduciary is paying the cost of his own "misconduct." [9]

More fundamentally, if the decision below is left in place, the Secretary will be shielded from any challenges by petitioners to the validity of his own apparent decision to require dual accounting under these leases. If the decision below is reversed, by contrast, the new policy requiring dual accounting will be highly suspect. It will come on the heels of nearly three decades of contrary practice— and thus will require a much more cogent jus-

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discussion of the principle that fiduciaries—not third parties—are generally responsible for the damages caused by their own breaches of fiduciary duty. He does not even attempt to distinguish *Nevada v. United States*, 463 U.S. 110, 144 n.16 (1983), which applied this principle to a breach of duty by the Secretary in his representation of Indians in a water-rights dispute. In any event, as discussed in the petitions, no meaningful distinction could be drawn.

[9] We note that the Tribe's claim for damages against the Government in the present dispute has been stayed pending the outcome of this case. *Jicarilla Apache Tribe v. United States*, No. 112-77 (Cl. Ct.).

tification than the Secretary has heretofore provided. Indeed, petitioners could then argue that the acceptance of a different royalty system by all parties for many years is itself sufficient to resolve any ambiguities in their favor.[10] In addition, the Secretary would be forced to explain why his policy concerning these leases differs sharply from the practice everywhere else. He would have to produce some justification other than the fact that these particular leases are the subject of litigation.

Each of these factors may help to explain the anomalous positions adopted by the Secretary in this Court. Neither, however, provides any valid reason for deferring consideration of the important issues raised here to some later case.

5. The Tribe offers two additional reasons why review should be denied here. Both are specious. First, the Tribe seeks to reintroduce into this case the notion that the contracts between the lessees and their customers were not "arms-length" and thus had the effect of reducing royalties due to the Tribe under the "BTU-adjustment" method. This argument was flatly rejected on the facts by the District Court after a full trial. The

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[10] Unlike the Secretary, the Tribe at least acknowledges our argument that the proper interpretation of the leases and regulations, based on original intent, can be derived from the fact that petitioners made nearly thirty years of supervised royalty payments without dual accounting. *See Mountain States Tel. & Tel. Co. v. Pueblo of Santa Ana*, 105 S. Ct. 2587 (1985). The Tribe's response is an attempt to show that the Secretary never looked at the issue prior to 1979. However, this argument is contradicted by the Secretary's explanation of why he *deliberately* rejected dual accounting prior to 1979. Opp. at 6 n.4. The Tenth Circuit also acknowledged that the Secretary had a clear *policy* against dual accounting during this period. J.A. 42a ("At the time this litigation began, the Secretary used the BTU method to calculate royalties due the Tribe.") *See also In re Supron Energy Corp. et al.* (No. 79-374, Interior Board of Land Appeals, March 21, 1980) (affirming the Area Supervisor's decision to impose dual accounting for the years 1974-76 solely on the lessee that had an interest in the processing plant in those years).

court found that the contracts at issue were arms-length and that any relationships among some of the corporations involved did not affect the prices paid. J.A. 114a.

Second, the Tribe refers to the fact that the Secretary is presently considering revised mineral lease regulations. But this fact is equally irrelevant. The proposed revisions neither moot the issues presented here nor support the argument for dual accounting. More fundamentally, as long as the decision below is in place, any new rules or lease terms would be subject to the same erroneous analysis of fiduciary duty that determined the outcome here.

CONCLUSION

The petitions for a writ of certiorari should be granted.

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BRIEF OF AMICI CURIAE IN SUPPORT OF PETITIONS FOR CERTIORARI

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Respondents.

BRIEF OF AMICI CURIAE IN SUPPORT OF PETITIONS FOR CERTIORARI

Pursuant to Rule 36 of the Rules of this Court and with the consent of all parties, Conoco Inc. and Tenneco Oil Company ("Producers") respectfully file this brief *amici curiae* in support

of the petitions for a writ of certiorari which seek review of the decision of the Tenth Circuit on rehearing *en banc* entered on January 23, 1986, (4-3), and supplemented on June 18, 1986.

INTEREST OF AMICI

The petitions raise three questions of great importance to Producers. First, the *en banc* decision by a divided Tenth Circuit below (4-3) imposes liability retroactively against innocent producer-lessees who had acted in reasonable reliance upon the conduct of the Secretary. *Amici* concur in petitioners' view that the common law trust principles relied upon by the Court in *United States* v. *Mitchell,* 463 U.S. 206, 226 (1983) ("Mitchell II") and *Nevada* v. *United States.* 463 U.S. 110, 145 (1983) ("Nevada") support that innocent third parties should not be held accountable for a trustee's breach of fiduciary obligations. [1]

Second, the majority decision on rehearing *en banc* below concludes that the District Court can set aside, as being arbitrary and capricious, the Secretary's long-standing determination as to the manner in which royalties should be computed for "wet" gas.[2] Under the Secretary's consistent and long-standing construction of standard lease terms and regulations, gas royalties were based upon the liquid products derived from the "wet" gas stream *only if* (i) the producer-lessee is the owner of the gas processing plant producing products from the wet gas stream, or

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[1] We note that the District Court correctly found that any failure by the producer-lessees to account for and pay royalties resulted from "no apparent fault of their own". Jt. App. 127a, 479 F.Supp. at 549. See also the discussion in the *en banc* dissenting opinion of Judges Seth, McWilliams and Barrett. Jt. App. 12a, 782 F.2d at 861.

[2] "Wet" natural gas is of such Btu content that it includes hydrocarbon substances in sufficient quantities that when processed through a plant, liquid by-products result. Wet gas has not been defined by the Secretary. The United States Geological Conservation Manual, Part 647, Chapter 2 (1977) however, defined "dry" gas as gas which contained minor amounts of liquefiable hydrocarbons, i.e., gas of 1050 Btu's or less at 14.73 psia and 60°F.

(ii) the producer-lessee realizes direct income from the sale of the liquid products derived from the wet gas stream. We concur with the decision by the original panel of the Tenth Circuit in that regard. In such opinion, Chief Judge Seth concludes that the Secretary's long-standing construction of the lease and the regulations was proper, especially given the express grant of authority to the Secretary which is contained in the lease. Jt. App. 28a-29a, 728 F.2d at 1559.

Third, the *en banc* majority's opinion below conflicts with the decisions of this Court in the *Mitchell II* and *Nevada* cases, *supra*, and the provisions of the Indian Mineral Leasing Act, 25 U.S.C. §§ 396(a) - 396(g) (1982) prescribing how the Secretary's trust duties to Indians must be defined. The majority's decision below in essence obligates the Secretary to "maximize" the Tribes' revenues over the short-term by resolving every ambiguity in a regulation or lease form in favor of the affected Tribe. We believe, instead, as stated in the *en banc* dissenting opinion of Judges Seth, McWilliams and Barrett, that the Secretary has discretion in carrying out his duties to carry out national resource development and energy policies. Jt. App. 5a, 782 F.2d at 857.

The interest of *Amici* in these issues is clear. Both are defendants in certain companion litigation being brought by the Jicarilla Apache Tribe, respondent herein; such litigation being *Jicarilla Apache Tribe* v. *Conoco Inc., et al.*, Civ. No. 76-430 (D.N.M.) (Complaint filed July 28, 1976). Testimony in the trial of such case was completed on August 4, 1984; and the decision of the trial court is *sub judice*. Conoco Inc. is also a defendant in a lawsuit pending in the United States District Court for the District of Wyoming, entitled *Shoshone and Arapahoe Indian Tribes* v. *Donald P. Hodel, et al.*, Civ. No. C81-131K (D. Wyo.) (Complaint filed Jan. 19, 1981).

In each of these two related litigation matters, issues similar to those herein are involved concerning (i) the Secretary's long-

standing uniform and reasonable interpretation of the terms of Standard Lease Form 5-157 and the regulations implementing the Indian Mineral Leasing Act; and (ii) the imposition of liability upon innocent producer-lessees which had acted in reasonable reliance upon the conduct of the Secretary.

STATEMENT OF THE CASE

Except as supplemented below, *Amici* adopt and incorporate by reference the statement of the case as set forth in the petition of Unicon Producing Company in Case No. 86-226.

We emphasize, however, that the primary issue on rehearing *en banc* before the Tenth Circuit was whether the Secretary's long-standing and pre-litigation construction of the provisions of Standard Lease Form 5-157 and his regulations were correct with respect to the computation and payment of royalties for "wet" gas. Under the Secretary's pre-litigation construction, if the producer-lessee did not, in fact, process the gas or own an interest in the gas processing plant, or otherwise directly receive "proceeds" from the processing of the natural gas, gas royalties were not to be based upon the plant product values. There was no finding by the District Court that the Secretary had acted in an arbitrary or capricious manner in reaching and continuing his construction of the standard lease terms and regulations as to the royalties to be paid for the "wet" natural gas at issue.

We observe, also, that in large part, the issues actually tried in the bench trial before the District Court concerned the purported antitrust claims being asserted by the plaintiff, Jicarilla Apache Tribe ("Tribe"), against the defendant producer-lessees. Such antitrust claims were dismissed by the District Court, and both the majority and minority opinions below are in full agreement that the Tribe wholly failed to sustain such antitrust claims.

SUMMARY OF ARGUMENT

The importance of the issues in this case to the management of both public lands and Indian lands is evident from the sharply divided *en banc* decision (4-3) of the Tenth Circuit as to which review is sought. An early and definitive ruling by the Court as to standards of review which apply to actions by the Secretary of the Interior regarding natural gas royalties to the Indians under the standard form oil and gas leases at issue is of great importance, especially given the ongoing litigation in which similar issues are being raised.

The *en banc* majority's decision below is inconsistent with the Secretary's long-standing interpretation of terms contained in a standard lease form and the regulations implementing the Indian Mineral Leasing Act. In addition, the determination of the *en banc* majority to impose liability upon innocent third-party producer-lessees is in direct conflict with the common law trust principles referred to by this Court in *Mitchell II*, *supra*, and *Nevada*, *supra*.

ARGUMENT

I.

THE PLAINTIFF INDIAN TRIBE FAILED TO PROVE THAT THE SECRETARY'S CONDUCT WAS ARBITRARY AND CAPRICIOUS, CONSTITUTED AN ABUSE OF DISCRETION, OR AMOUNTED TO A BREACH OF TRUST.

With respect to the claims of the Tribe against the defendant producer-lessees, the underlying oil and gas leases are standard forms issued by the Federal Government. Jt. App. 61a-62a, 728 F.2d at 1574-1575. The pertinent provisions of such Standard Lease Form 5-157 provide as follows:

> [T]he Lessee hereby agrees . . .
>
> * * *

> — To pay . . . a royalty of 16⅔ percent of the value or amount of all oil, gas . . . and/or all other hydrocarbon substances produced and saved from the land leased herein . . . . During the period of supervision, "value" for the purposes hereof may, in the discretion of the Secretary, be calculated on the basis of the highest price paid or offered (whether calculated on the basis of short or actual volume) at the time of production for the major portion of the oil of the same gravity, and gas and/or natural gasoline, and/or all other hydrocarbon substances produced and sold from the field where the leased lands are situated, and the actual volume of the marketable product less the content of foreign substances as determined by the oil and gas supervisor. *The actual amount realized by the lessee from the sale of said products may, in the discretion of the Secretary, be deemed mere evidence of conclusive evidence of such value.* (emphasis added.)[3]

Under the terms of the applicable leases, therefore, the Secretary explicitly is authorized to use his discretion to accept the "actual amount realized by the Lessee from the sale of said products" (i.e., natural gas) as "conclusive evidence" of value for natural gas production for purposes of computation and payment of royalties.[4] No evidence was presented before the trial court which establishes that the Secretary either abused his discretion or acted in an arbitrary and capricious manner by having used the actual proceeds which accrued to the defendant producer-lessees under long-term gas sales contracts as constituting "value" for gas royalty computation and payment purposes.

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[3] We have underlined the word "all" to emphasize that nothing in the Standard Lease Form 5-157 authorizes the Secretary of the Interior, or his designees, to "value" the Government's proportionate share (i.e., the 16⅔ percentage share) at a value or amount different from that of the share of the producer-lessee.

[4] We note that decision by the majority of the original panel of the Tenth Circuit expressly discusses this issue. Jt. App. 28a-29a, 728 F.2d at 1559-60.

It must be presumed by this Court, furthermore, that the Secretary of the Interior, government accountants, and other public officials not only properly performed their duties, but also faithfully discharged those matters committed to their discretion under the applicable laws and regulations.[5] *First Nat'l Bank in Billings* v. *First Bank Stock Corp.*, 197 F. Supp. 417, 424-25 (D. Mont. 1961); Fed. R. Evid., Rule 301 (1982); 1 Jones on Evidence § 3:34 (1972); Annot., Presumption That Public Officers Have Properly Performed Their Duties, As Evidence, 141 A.L.R. 1037 (1942); and the *en banc* dissenting opinion of Judges Seth, McWilliams and Barrett at Jt. App. 5a, 782 F.2d 857.

It should be noted, moreover, that the Secretary filed a brief in the companion litigation styled *Jicarilla Apache Tribe* v. *Conoco Inc.*, No. 76-430 (D.N.M.) fully supporting the decision of the original panel of the Tenth Circuit. In such brief of the Government, it is stated that the Secretary's observance of long-standing administrative practice, and his failure to have immediately changed the royalty computation practices as to gas produced from the Jicarilla Reservation Lands was "neither arbitrary and capricious nor an abuse of discretion or a breach of trust . . . " (Federal Defendant's Supp. Brief dated April 2, 1984, at Page 3.)[6]

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[5] Under the United States Geological Survey ("USGS") Conservation Division Manual, Part 647, Chapter 2 (1977), it is specified that the area accountant "is responsible for . . . ensuring that royalties are timely and correctly billed . . . (and) ensuring that required audits and notifications are made." (reference added). Trial testimony contained in the Joint Appendix as filed with the Tenth Circuit confirms that the USGS Accountants involved properly performed their duties and followed the existing regulations and long-standing administrative construction of the lease provisions. (10th Cir. App. A-932 to 934).

[6] We note, parenthetically, that the Tribe also has filed an action for money damages against the Secretary of the Interior. Jt. App. 41a, n.3. That action has been stayed pending the outcome of this suit. Judges Seth, McWilliams, and Barrett expressly have dissented

The Secretary and the subagencies within the United States Department of the Interior prior to the commencement of this litigation, moreover, had followed a long-standing and consistent practice of having interpreted the word "value" under various government standard oil and gas lease forms to mean the actual proceeds accruing to lessees under long-term natural gas sales contracts. With regard to this long-standing administrative construction and policy of using actual proceeds accruing to the lessee under arms-length gas sales contracts as constituting "value", see: ABA Natural Resources Law Section — Task Force Report on Federal Oil and Gas Royalty Matters, 15 Nat. Resources Law., 757 at 762, 782 (1983) (referring to the long history within the United States Department of the Interior of having accepted the proceeds accruing to the lessee under gas sales contracts as being the proper measure for royalty value); Testimony of Jack Darrough, USGS, Supervisor Accountant, at p. A-933 of the Joint Appendix filed with the Tenth Circuit (referring to the past practice within the USGS of having computed royalties based on the "contract price or on prices allowed by F.P.C. . . . ."); USGS Conservation Division Manual, Part 647, Chapter 2, 647.2.1, Exh. No. 1, Historical Information (Release No. 35, Aug. 15, 1977) (stating that the USGS historically operated under a *policy* that "royalty was generally based on the price received by the Lessee under an arms-length contract . . . .").

Corporations such as the defendant producer-lessees are "persons", after all, for purposes of the constitutional guarantees of due process and just compensation. *Louis K. Liggett Co.* v. *Baldridge*, 278 U.S. 105, 111 (1928); *Jim Young Development Corp.* v. *State Highway Comm'n*, 56 F.R.D. 38, 41 (W.D. Mo.

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from the *en banc* majority's conclusion that the defendant producer-lessees should pay the additional royalties due if the nonpayment resulted from the Government's breach of its fiduciary duty. Jt. App. 5a, 782 F.2d at 857.

1971). The Fifth Amendment protects the property of corporations against confiscation equally with that of individuals. *County of San Mateo* v. *Southern Pacific R.R. Co.*, 13 Fed. 145 (C.C. Cal. 1882). Corporations are possessed of the same guarantees of constitutional property rights as natural persons. *Pierce* v. *Society of Sisters*, 268 U.S. 510 (1925). The protections from arbitrary power and arbitrary legislation are basic among the constitutional protections afforded by the due process requirement. *Heiner* v. *Donnan*, 285 U.S. 312 (1932). A leasehold interest is a property right which may not be appropriated by governmental action without just compensation. *Sun Oil Co.* v. *United States*, 572 F.2d 786, 818 (Ct. Cl. 1978). Government regulations can become so onerous as to constitute a taking which requires just compensation. *Goldblatt* v. *Town of Hempstead*, N.Y., 369 U.S. 590 (1962).

A sudden change by the Secretary or government subagencies in the procedures for fixing value of natural gas production and its derivative products for royalty purposes would constitute a violation of due process. *King* v. *Finch*, 428 F.2d 709, 713 (5th Cir. 1970). *Baltimore & Annapolis R.R. Co.* v. *Washington Metro. Area Transit*, 642 F.2d 1365, 1370 (D.C. Cir. 1980). In the instant situation, moreover, the long-standing administrative practice and findings by the Secretary as to royalty valuation are a rule of property; and to change such procedures "retroactively" would be arbitrary, capricious, and violative of due process guarantees. *Amoco Production Co.* v. *Andrus*, 527 F. Supp. 790 (E.D. La. 1981); *Marathon Oil Co.* v. *Andrus*, 452 F. Supp. 548 (D. Wyo. 1978); *cf.*, *Utah International Inc.* v. *Andrus*, 488 F. Supp. 976 (D. Colo. 1980).

In short, under the circumstances neither the Minerals Management Service nor the Secretary lawfully could retroactively change the methods used for fixing and determining the value of gas or gas products for royalty computation and payment purposes. *Continental Oil Co.* v. *United States*, 184 F.2d 802, 821

(9th Cir. 1950) (holding that the Secretary may neither retroactively recompute royalties nor make retroactive an order which changes the method to be used for fixing the value of natural gas and its derivative products for royalty purposes). Accordingly, the majority opinion by the original panel of this Court is legally correct in its holding that the pre-litigation administrative interpretation and construction of the leases and regulations concerning computation of gas royalties by the Secretary "must be applied to and through the conclusion of these proceedings." Jt. App. 29a, 728 F.2d at 1560.

II.

THE DECISION OF THE MAJORITY BELOW CONFLICTS WITH PRIOR DECISIONS OF THIS COURT WHICH HOLD THE SECRETARY AS TRUSTEE, AND NOT INNOCENT THIRD PARTIES, LIABLE FOR ALLEGED BREACHES OF TRUST.

After the subject oil and gas leases were entered into, the Secretary issued monthly "Statements of Account" (USGS Form 9-1424) to the defendant producer-lessees (App. A-934, A-101).[7] These monthly statements of account as issued by the

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[7] 30 C.F.R. § 221.40 (1975) states in part: "[T]he lessee shall tender all payments of . . . royalty . . . in accordance with the statements rendered by the Supervisor pursuant to § 221.12 . . . ."

30 C.F.R. 221.12 (1975) states in part: "The Supervisor shall render monthly to the lessee . . . statements showing the amount of . . . gas produced or sold and the . . . *value* of production accruing to the lessor as royalty. (emphasis added)

See also with regard to payment of royalties by lessees in conformity with billings and determinations made by the Secretary of the Interior: USGS Conservation Division Manual Part 647, Chapters 2 and 15; Notice to Lessees and Operators of Indian Oil and Gas Leases (NTL-1A), 42 Fed. Reg. 4546 (Jan. 25, 1977); Notice to Lessees and Operators of Federal and Indian Onshore Oil and Gas Leases (NTL-5), 42 Fed. Reg. 22610 (Mar. 4, 1977); Testimony of Jack Darrough, USGS Accountant at App. A-932 to A-934 of the Joint Appendix as filed with the Tenth Circuit in this

Secretary set forth, among other things, the "value" of the natural gas production identified therein for royalty computation and payment purposes. The defendant lessees relied upon the issuance to them of these "statements of account" by the Secretary as constituting a confirmation of the value and determination of the royalties applicable to the natural gas production being referred to in such statements.

An examination of the "pre-litigation" statement of account forms (USGS Form 9-1424) which were sent to the Lessees of Indian oil and gas leases by the Secretary confirms that such were "account statements" or "billings" in every sense. For example, such statement of account forms directed Lessees to "remit by check, draft, or money order" any amount shown to be due. The third column is "lease value", and the last column is "charges and payments." Like any ordinary billing, these statements concluded: "The last item is your balance." The rendition of these monthly statements or billings by the USGS to the defendant lessees, we submit, constituted an official act by the Secretary. 30 C.F.R. §§ 221.12, 221.40 (1975); 25 C.F.R. § 171.13 (1975); Jt. App. 68a.

In issuing these account statements, the Secretary, or his representatives, computed "value" and the resulting royalties based upon the prices received by the producer-lessee under the applicable gas sales contract or the prices allowed by the Federal Power Commission, or its successor, the Federal Energy Regulatory Commission. (See page A-933 of the Joint Appendix as filed with the Tenth Circuit.)

It was not until after the Jicarilla Apache Tribe commenced this litigation in 1975, in fact, that the Secretary added a *new* legend at the bottom of the monthly statement of account form

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case; Memorandum Opinion filed September 7, 1978 (Mechem, J.) in this case, Jt. App. 68a-69a.

issued to lessees.[8] The new legend added by the Secretary was to the effect that the information being provided to the lessees in the statement of account form was "subject to correction". Such post-litigation addition of this cautionary legend, we submit, was nothing more than a self-serving maneuver by the Secretary, done at the urging and insistence of the Tribe. This conduct by the Secretary only serves to emphasize the prejudicial effect upon the claims being asserted against the defendant producer-lessees which results from the Government-Lessor having regularly issued the statements of account.[9]

The majority decision below appears to clearly impose liabilities upon producer-lessees who acted in reasonable reliance upon the Secretary's administration of oil and gas leases, including the Secretary's issuance of valuation determination as represented in the monthly statements of account given to such lessees. This holding conflicts with the statements of this Court in *Mitchell II, supra,* wherein this Court stated:

> Given the existence of a trust relationship, it naturally follows that the Government should be liable in damages for the breach of its fiduciary duties. It is well established that a trustee is accountable in damages for breaches of trust. *See* Restatement (Second) of Trusts §§ 205-212 (1959); G. Bogert, Law of Trusts and Trustees § 862 (2d ed. 1965); 3 A. Scott, Law of Trusts § 205 (3d ed. 1967). 463 U.S. at 226-27.

The majority *en banc* opinion below, moreover, imposed liability upon the innocent producer-lessees despite the fact that the District Court had expressly concluded that any failure to account

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[8] A photostatic copy of a USGS Form 9-1424 (rev. 12-68) as rendered in 1972 by the United States Department of Interior, Geological Survey to lessees under Indian oil and gas leases is contained in the Annex to this brief at p. 1a, *infra.*

[9] We note, parenthetically, that "dual accounting" also came about only after the litigation had been commenced. See the discussion by Judges Seth, McWilliams, and Barrett in the dissenting *en banc* opinion. Jt. App. 13a, 782 F.2d at 861.

and pay for royalties resulted from "no apparent fault" of the producer-lessees. Jt. App. 127a, 479 F. Supp. 549.[10]

The common law principles referred to by this Court in both *Mitchell II, supra,* and *Nevada, supra,* support the proposition that innocent third party producer-lessees should not be held accountable for a trustee's alleged breaches of fiduciary obligations. *See,* Restatement (Second) of Trusts § 326 (1959) (third parties liable to a beneficiary only if they have notice of a breach and participate in it); see, also, A. Scott, the Law of Trusts §§ 321, 326, 326.1, 326.6 (2d ed. 1956); *International State Bank* v. *Bray,* 87 N.M. 350, 352, 533 P.2d 583, 585 (1975); *Voss Oil Co.* v. *Voss,* 367 P.2d 977, 980 (Wyo. 1962).

[10] See also the discussion in the memorandum opinion of the District Court filed September 7, 1978. Jt. App. 68a-69a.

CONCLUSION

As is evidenced by the sharply divided decision of the Tenth Circuit below (4–3), this case raises important questions concerning the administration of Indian lands. Because the majority decision below conflicts with the principles announced by the Court in *Mitchell II, supra,* and *Nevada, supra,* the terms of the lease agreements at issue, and settled principles of trust law, certiorari should be granted.

Respectfully submitted,

s/ Ernest J. Altgelt, III

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CERTIFICATE OF SERVICE

I hereby certify that I caused a true and correct copy of the foregoing Brief of Amici Curiae In Support of Petitions For Certiorari to be mailed, by placing same in the United States mail, postage prepaid, to the following counsel of record on the 25th day of August, 1986.

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ANNEX

ANNEX

STATEMENT OF ACCOUNT

UNITED STATES
DEPARTMENT OF THE INTERIOR
GEOLOGICAL SURVEY

ISSUING OFFICE: 1
REGIONAL SUPERVISOR
CONSERVATION DIVISION

ACCOUNT NO. 35 14-20-258-001348 WYOMING
IND TRIBAL LAND FIELD 713

2002 FEDERAL BUILDING
P. O. BOX 2859
CASPER, WYOMING 82601

1

CONTINENTAL OIL CO
DRAWER 1267
PONCA CITY, OK 74601

185

2

JOINT BUSINESS COUNCIL
FT WASHAKIE, WY

REMIT BY CHECK, DRAFT OR MONEY ORDER						NO RECEIPT WILL BE ISSUED		
STATEMENT FOR MONTH ENDING 12/31/71					BALANCE FROM THE PREVIOUS STATEMENT		- 0 -	45.02
EXPLANATION (QUANTITIES REPORT BARRELS OF OIL, THOUSANDS OF CUBIC FEET OF GAS, BARRELS OF GASOLINE AND LIQUID HYDROCARBONS AND TONS)					LEASE QUANTITY	LEASE VALUE ROYALTY QUANTITY (TO 3 DECIMALS)	UNAPPLIED RENTAL	CHARGES AND PAYMENTS
GAS	ADJ977	512	07/70		140,172.00	21,780.77		3,630.13
GAS	ADJ977	512	07/70		140,172.00CR	21,750.39CR		3,625.07
GAS	ADJ977	512	08/70		155,770.00	24,204.48		4,034.08
GAS	ADJ977	512	08/70		155,770.00CR	24,003.80CR		4,000.63
GAS	977	840	11/71		267,714.00	45,423.84		7,570.64
OIL	977	963	12/71		2,664.47	8,473.03		1,412.17
GAS	977	963	12/71		270,501.00	45,195.15		7,532.53
PAID 11/71 GAS 185 X342 08 01/06/72								38.51
PAID 11/71 GAS 185 X342 08 01/06/72								7,570.66
PAID 11/71 GAS 185 X361 08 01/31/72								7,532.66
						BALANCE	- 0 -	1,457.02

CHECK OR DRAFT PAYABLE TO UNITED STATES GEOLOGICAL SURVEY AND FORWARDED TO ISSUING OFFICE ABOVE EXCEPT WHEN DATA, PETROLEUM RESERVE NO. 2 AND INDIAN PURCHASES. SHALL BE MADE IN ACCORDANCE WITH SPECIFIC INSTRUCTIONS FROM ISSUING OFFICE

LAST ITEM IS YOUR BALANCE

CORRECTED COPY

CORRECTED

Nos. 86-219, 86-224, 86-225, 86-226

Supreme Court, U.S.
FILED
AUG 25 1986
JOSEPH F. SPANIOL, JR.
CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1986

SOUTHERN UNION CO., ET AL.,
Petitioner.

v.

JICARILLA APACHE TRIBE, ET AL.,
Respondents.

SOUTHLAND ROYALTY COMPANY
Petitioner,

v.

JICARILLA APACHE TRIBE AND DONALD P. HODEL, SECRETARY OF THE INTERIOR,
Respondents.

EXXON CORPORATION, *et al.*,
Petitioner,

v.

JICARILLA APACHE TRIBE, ET AL.,
Respondents.

UNICON PRODUCING CO.,
Petitioner,

v.

JICARILLA APACHE TRIBE, ET AL.,
Respondents.

BRIEF OF AMICI CURIAE IN SUPPORT OF PETITIONS FOR CERTIORARI

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Fed. R. Evid., Rule 301 (1982) 7
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Notice to Lessees and Operators of Federal and Indian Onshore Oil and Gas Leases (NTL-5), 42 Fed. Reg. 22610 (March 4, 1977) .....)
1 Jones on Evidence § 3:34 (1972) 7
Restatement (Second) of Trusts § 326 (1959) 13
A. Scott, The Law of Trusts §§ 321, 326, 226.1, 326.6 (2d ed. 1956) 13
USGS Conservation Division Manual Part 647, Chapter 2 (1977) 2, 6, 8, 10

Nos. 86-219, 86-224, 86-225, 86-226

IN THE

Supreme Court of the United States

OCTOBER TERM, 1986

SOUTHERN UNION CO., ET AL.,

Petitioner.

v.

JICARILLA APACHE TRIBE, ET AL.,

Respondents.

SOUTHLAND ROYALTY COMPANY

Petitioner,

v.

JICARILLA APACHE TRIBE AND DONALD P. HODEL, SECRETARY OF THE INTERIOR,

Respondents.

EXXON CORPORATION, *et al.*,

Petitioner,

v.

JICARILLA APACHE TRIBE, ET AL.,

Respondents.

UNICON PRODUCING CO.,

Petitioner,

v.

JICARILLA APACHE TRIBE, ET AL.,

Respondents.

BRIEF OF AMICI CURIAE IN SUPPORT OF PETITIONS FOR CERTIORARI

Pursuant to Rule 36 of the Rules of this Court and with the consent of all parties, Conoco Inc. and Tenneco Oil Company ("Producers") respectfully file this brief *amici curiae* in support

of the petitions for a writ of certiorari which seek review of the decision of the Tenth Circuit on rehearing *en banc* entered on January 23, 1986, (4-3), and supplemented on June 18, 1986.

INTEREST OF AMICI

The petitions raise three questions of great importance to Producers. First, the *en banc* decision by a divided Tenth Circuit below (4-3) imposes liability retroactively against innocent producer-lessees who had acted in reasonable reliance upon the conduct of the Secretary. *Amici* concur in petitioners' view that the common law trust principles relied upon by the Court in *United States* v. *Mitchell*, 463 U.S. 206, 226 (1983) ("Mitchell II") and *Nevada* v. *United States*. 463 U.S. 110, 145 (1983) ("Nevada") support that innocent third parties should not be held accountable for a trustee's breach of fiduciary obligations. [1]

Second, the majority decision on rehearing *en banc* below concludes that the District Court can set aside, as being arbitrary and capricious, the Secretary's long-standing determination as to the manner in which royalties should be computed for "wet" gas.[2] Under the Secretary's consistent and long-standing construction of standard lease terms and regulations, gas royalties were based upon the liquid products derived from the "wet" gas stream *only if* (i) the producer-lessee is the owner of the gas processing plant producing products from the wet gas stream, or

---

[1] We note that the District Court correctly found that any failure by the producer-lessees to account for and pay royalties resulted from "no apparent fault of their own". Jt. App. 127a, 479 F.Supp. at 549. See also the discussion in the *en banc* dissenting opinion of Judges Seth, McWilliams and Barrett. Jt. App. 12a, 782 F.2d at 861.

[2] "Wet" natural gas is of such Btu content that it includes hydrocarbon substances in sufficient quantities that when processed through a plant, liquid by-products result. Wet gas has not been defined by the Secretary. The United States Geological Conservation Manual, Part 647, Chapter 2 (1977) however, defined "dry" gas as gas which contained minor amounts of liquefiable hydrocarbons, i.e., gas of 1050 Btu's or less at 14.73 psia and 60°F.

(ii) the producer-lessee realizes direct income from the sale of the liquid products derived from the wet gas stream. We concur with the decision by the original panel of the Tenth Circuit in that regard. In such opinion, Chief Judge Seth concludes that the Secretary's long-standing construction of the lease and the regulations was proper, especially given the express grant of authority to the Secretary which is contained in the lease. Jt. App. 28a-29a, 728 F.2d at 1559.

Third, the *en banc* majority's opinion below conflicts with the decisions of this Court in the *Mitchell II* and *Nevada* cases, *supra*, and the provisions of the Indian Mineral Leasing Act, 25 U.S.C. §§ 396(a) - 396(g) (1982) prescribing how the Secretary's trust duties to Indians must be defined. The majority's decision below in essence obligates the Secretary to "maximize" the Tribes' revenues over the short-term by resolving every ambiguity in a regulation or lease form in favor of the affected Tribe. We believe, instead, as stated in the *en banc* dissenting opinion of Judges Seth, McWilliams and Barrett, that the Secretary has discretion in carrying out his duties to carry out national resource development and energy policies. Jt. App. 5a, 782 F.2d at 857.

The interest of *Amici* in these issues is clear. Both are defendants in certain companion litigation being brought by the Jicarilla Apache Tribe, respondent herein; such litigation being *Jicarilla Apache Tribe* v. *Conoco Inc., et al.*, Civ. No. 76-430 (D.N.M.) (Complaint filed July 28, 1976). Testimony in the trial of such case was completed on August 4, 1984; and the decision of the trial court is *sub judice*. Conoco Inc. is also a defendant in a lawsuit pending in the United States District Court for the District of Wyoming, entitled *Shoshone and Arapahoe Indian Tribes* v. *Donald P. Hodel, et al.*, Civ. No. C81-131K (D. Wyo.) (Complaint filed Jan. 19, 1981).

In each of these two related litigation matters, issues similar to those herein are involved concerning (i) the Secretary's long-

standing uniform and reasonable interpretation of the terms of Standard Lease Form 5-157 and the regulations implementing the Indian Mineral Leasing Act; and (ii) the imposition of liability upon innocent producer-lessees which had acted in reasonable reliance upon the conduct of the Secretary.

STATEMENT OF THE CASE

Except as supplemented below, *Amici* adopt and incorporate by reference the statement of the case as set forth in the petition of Unicon Producing Company in Case No. 86-226.

We emphasize, however, that the primary issue on rehearing *en banc* before the Tenth Circuit was whether the Secretary's long-standing and pre-litigation construction of the provisions of Standard Lease Form 5-157 and his regulations were correct with respect to the computation and payment of royalties for "wet" gas. Under the Secretary's pre-litigation construction, if the producer-lessee did not, in fact, process the gas or own an interest in the gas processing plant, or otherwise directly receive "proceeds" from the processing of the natural gas, gas royalties were not to be based upon the plant product values. There was no finding by the District Court that the Secretary had acted in an arbitrary or capricious manner in reaching and continuing his construction of the standard lease terms and regulations as to the royalties to be paid for the "wet" natural gas at issue.

We observe, also, that in large part, the issues actually tried in the bench trial before the District Court concerned the purported antitrust claims being asserted by the plaintiff, Jicarilla Apache Tribe ("Tribe"), against the defendant producer-lessees. Such antitrust claims were dismissed by the District Court, and both the majority and minority opinions below are in full agreement that the Tribe wholly failed to sustain such antitrust claims.

SUMMARY OF ARGUMENT

The importance of the issues in this case to the management of both public lands and Indian lands is evident from the sharply divided *en banc* decision (4-3) of the Tenth Circuit as to which review is sought. An early and definitive ruling by the Court as to standards of review which apply to actions by the Secretary of the Interior regarding natural gas royalties to the Indians under the standard form oil and gas leases at issue is of great importance, especially given the ongoing litigation in which similar issues are being raised.

The *en banc* majority's decision below is inconsistent with the Secretary's long-standing interpretation of terms contained in a standard lease form and the regulations implementing the Indian Mineral Leasing Act. In addition, the determination of the *en banc* majority to impose liability upon innocent third-party producer-lessees is in direct conflict with the common law trust principles referred to by this Court in *Mitchell II, supra,* and *Nevada, supra.*

ARGUMENT

I.

THE PLAINTIFF INDIAN TRIBE FAILED TO PROVE THAT THE SECRETARY'S CONDUCT WAS ARBITRARY AND CAPRICIOUS, CONSTITUTED AN ABUSE OF DISCRETION, OR AMOUNTED TO A BREACH OF TRUST.

With respect to the claims of the Tribe against the defendant producer-lessees, the underlying oil and gas leases are standard forms issued by the Federal Government. Jt. App. 61a-62a, 728 F.2d at 1574-1575. The pertinent provisions of such Standard Lease Form 5-157 provide as follows:

> [T]he Lessee hereby agrees . . .
>
> * * *

> — To pay . . . a royalty of 16⅔ percent of the value or amount of all oil, gas . . . and/or all other hydrocarbon substances produced and saved from the land leased herein . . . . During the period of supervision, "value" for the purposes hereof may, in the discretion of the Secretary, be calculated on the basis of the highest price paid or offered (whether calculated on the basis of short or actual volume) at the time of production for the major portion of the oil of the same gravity, and gas and/or natural gasoline, and/or all other hydrocarbon substances produced and sold from the field where the leased lands are situated, and the actual volume of the marketable product less the content of foreign substances as determined by the oil and gas supervisor. *The actual amount realized by the lessee from the sale of said products may, in the discretion of the Secretary, be deemed mere evidence of or conclusive evidence of such value.* (emphasis added.)[3]

Under the terms of the applicable leases, therefore, the Secretary explicitly is authorized to use his discretion to accept the "actual amount realized by the Lessee from the sale of said products" (i.e., natural gas) as "conclusive evidence" of value for natural gas production for purposes of computation and payment of royalties.[4] No evidence was presented before the trial court which establishes that the Secretary either abused his discretion or acted in an arbitrary and capricious manner by having used the actual proceeds which accrued to the defendant producer-lessees under long-term gas sales contracts as constituting "value" for gas royalty computation and payment purposes.

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[3] We have underlined the word "all" to emphasize that nothing in the Standard Lease Form 5-157 authorizes the Secretary of the Interior, or his designees, to "value" the Government's proportionate share (i.e., the 16⅔ percentage share) at a value or amount different from that of the share of the producer-lessee.

[4] We note that decision by the majority of the original panel of the Tenth Circuit expressly discusses this issue. Jt. App. 28a-29a, 728 F.2d at 1559-60.

It must be presumed by this Court, furthermore, that the Secretary of the Interior, government accountants, and other public officials not only properly performed their duties, but also faithfully discharged those matters committed to their discretion under the applicable laws and regulations.[5] *First Nat'l Bank in Billings* v. *First Bank Stock Corp.*, 197 F. Supp. 417, 424-25 (D. Mont. 1961); Fed. R. Evid., Rule 301 (1982); 1 Jones on Evidence § 3:34 (1972); Annot., Presumption That Public Officers Have Properly Performed Their Duties, As Evidence, 141 A.L.R. 1037 (1942); and the *en banc* dissenting opinion of Judges Seth, McWilliams and Barrett at Jt. App. 5a, 782 F.2d 857.

It should be noted, moreover, that the Secretary filed a brief in the companion litigation styled *Jicarilla Apache Tribe* v. *Conoco Inc.*, No. 76-430 (D.N.M.) fully supporting the decision of the original panel of the Tenth Circuit. In such brief of the Government, it is stated that the Secretary's observance of long-standing administrative practice, and his failure to have immediately changed the royalty computation practices as to gas produced from the Jicarilla Reservation Lands was "neither arbitrary and capricious nor an abuse of discretion or a breach of trust . . . " (Federal Defendant's Supp. Brief dated April 2, 1984, at Page 3.)[6]

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[5] Under the United States Geological Survey ("USGS") Conservation Division Manual, Part 647, Chapter 2 (1977), it is specified that the area accountant "is responsible for . . . ensuring that royalties are timely and correctly billed . . . (and) ensuring that required audits and notifications are made." (reference added). Trial testimony contained in the Joint Appendix as filed with the Tenth Circuit confirms that the USGS Accountants involved properly performed their duties and followed the existing regulations and long-standing administrative construction of the lease provisions. (10th Cir. App. A-932 to 934).

[6] We note, parenthetically, that the Tribe also has filed an action for money damages against the Secretary of the Interior. Jt. App. 41a, n.3. That action has been stayed pending the outcome of this suit. Judges Seth, McWilliams, and Barrett expressly have dissented

The Secretary and the subagencies within the United States Department of the Interior prior to the commencement of this litigation, moreover, had followed a long-standing and consistent practice of having interpreted the word "value" under various government standard oil and gas lease forms to mean the actual proceeds accruing to lessees under long-term natural gas sales contracts. With regard to this long-standing administrative construction and policy of using actual proceeds accruing to the lessee under arms-length gas sales contracts as constituting "value", see: ABA Natural Resources Law Section — Task Force Report on Federal Oil and Gas Royalty Matters, 15 Nat. Resources Law., 757 at 762, 782 (1983) (referring to the long history within the United States Department of the Interior of having accepted the proceeds accruing to the lessee under gas sales contracts as being the proper measure for royalty value); Testimony of Jack Darrough, USGS, Supervisor Accountant, at p. A-933 of the Joint Appendix filed with the Tenth Circuit (referring to the past practice within the USGS of having computed royalties based on the "contract price or on prices allowed by F.P.C. . . . ."); USGS Conservation Division Manual, Part 647, Chapter 2, 647.2.1, Exh. No. 1, Historical Information (Release No. 35, Aug. 15, 1977) (stating that the USGS historically operated under a *policy* that "royalty was generally based on the price received by the Lessee under an arms-length contract . . . .").

Corporations such as the defendant producer-lessees are "persons", after all, for purposes of the constitutional guarantees of due process and just compensation. *Louis K. Liggett Co.* v. *Baldridge*, 278 U.S. 105, 111 (1928); *Jim Young Development Corp.* v. *State Highway Comm'n*, 56 F.R.D. 38, 41 (W.D. Mo.

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from the *en banc* majority's conclusion that the defendant producer-lessees should pay the additional royalties due if the nonpayment resulted from the Government's breach of its fiduciary duty. Jt. App. 5a, 782 F.2d at 857.

1971). The Fifth Amendment protects the property of corporations against confiscation equally with that of individuals. *County of San Mateo* v. *Southern Pacific R.R. Co.*, 13 Fed. 145 (C.C. Cal. 1882). Corporations are possessed of the same guarantees of constitutional property rights as natural persons. *Pierce* v. *Society of Sisters*, 268 U.S. 510 (1925). The protections from arbitrary power and arbitrary legislation are basic among the constitutional protections afforded by the due process requirement. *Heiner* v. *Donnan*, 285 U.S. 312 (1932). A leasehold interest is a property right which may not be appropriated by governmental action without just compensation. *Sun Oil Co.* v. *United States*, 572 F.2d 786, 818 (Ct. Cl. 1978). Government regulations can become so onerous as to constitute a taking which requires just compensation. *Goldblatt* v. *Town of Hempstead*, N.Y., 369 U.S. 590 (1962).

A sudden change by the Secretary or government subagencies in the procedures for fixing value of natural gas production and its derivative products for royalty purposes would constitute a violation of due process. *King* v. *Finch*, 428 F.2d 709, 713 (5th Cir. 1970). *Baltimore & Annapolis R.R. Co.* v. *Washington Metro. Area Transit*, 642 F.2d 1365, 1370 (D.C. Cir. 1980). In the instant situation, moreover, the long-standing administrative practice and findings by the Secretary as to royalty valuation are a rule of property; and to change such procedures "retroactively" would be arbitrary, capricious, and violative of due process guarantees. *Amoco Production Co.* v. *Andrus*, 527 F. Supp. 790 (E.D. La. 1981); *Marathon Oil Co.* v. *Andrus*, 452 F. Supp. 548 (D. Wyo. 1978); *cf.*, *Utah International Inc.* v. *Andrus*, 488 F. Supp. 976 (D. Colo. 1980).

In short, under the circumstances neither the Minerals Management Service nor the Secretary lawfully could retroactively change the methods used for fixing and determining the value of gas or gas products for royalty computation and payment purposes. *Continental Oil Co.* v. *United States*, 184 F.2d 802, 821

(9th Cir. 1950) (holding that the Secretary may neither retroactively recompute royalties nor make retroactive an order which changes the method to be used for fixing the value of natural gas and its derivative products for royalty purposes). Accordingly, the majority opinion by the original panel of this Court is legally correct in its holding that the pre-litigation administrative interpretation and construction of the leases and regulations concerning computation of gas royalties by the Secretary "must be applied to and through the conclusion of these proceedings." Jt. App. 29a, 728 F.2d at 1560.

II.

THE DECISION OF THE MAJORITY BELOW CONFLICTS WITH PRIOR DECISIONS OF THIS COURT WHICH HOLD THE SECRETARY AS TRUSTEE, AND NOT INNOCENT THIRD PARTIES, LIABLE FOR ALLEGED BREACHES OF TRUST.

After the subject oil and gas leases were entered into, the Secretary issued monthly "Statements of Account" (USGS Form 9-1424) to the defendant producer-lessees (App. A-934, A-101).[7] These monthly statements of account as issued by the

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[7] 30 C.F.R. § 221.40 (1975) states in part: "[T]he lessee shall tender all payments of . . . royalty . . . in accordance with the statements rendered by the Supervisor pursuant to § 221.12 . . . ."

30 C.F.R. 221.12 (1975) states in part: "The Supervisor shall render monthly to the lessee . . . statements showing the amount of . . . gas produced or sold and the . . . *value* of production accruing to the lessor as royalty. (emphasis added)

See also with regard to payment of royalties by lessees in conformity with billings and determinations made by the Secretary of the Interior: USGS Conservation Division Manual Part 647, Chapters 2 and 15; Notice to Lessees and Operators of Indian Oil and Gas Leases (NTL-1A), 42 Fed. Reg. 4546 (Jan. 25, 1977); Notice to Lessees and Operators of Federal and Indian Onshore Oil and Gas Leases (NTL-5), 42 Fed. Reg. 22610 (Mar. 4, 1977); Testimony of Jack Darrough, USGS Accountant at App. A-932 to A-934 of the Joint Appendix as filed with the Tenth Circuit in this

Secretary set forth, among other things, the "value" of the natural gas production identified therein for royalty computation and payment purposes. The defendant lessees relied upon the issuance to them of these "statements of account" by the Secretary as constituting a confirmation of the value and determination of the royalties applicable to the natural gas production being referred to in such statements.

An examination of the "pre-litigation" statement of account forms (USGS Form 9-1424) which were sent to the Lessees of Indian oil and gas leases by the Secretary confirms that such were "account statements" or "billings" in every sense. For example, such statement of account forms directed Lessees to "remit by check, draft, or money order" any amount shown to be due. The third column is "lease value", and the last column is "charges and payments." Like any ordinary billing, these statements concluded: "The last item is your balance." The rendition of these monthly statements or billings by the USGS to the defendant lessees, we submit, constituted an official act by the Secretary. 30 C.F.R. §§ 221.12, 221.40 (1975); 25 C.F.R. § 171.13 (1975); Jt. App. 68a.

In issuing these account statements, the Secretary, or his representatives, computed "value" and the resulting royalties based upon the prices received by the producer-lessee under the applicable gas sales contract or the prices allowed by the Federal Power Commission, or its successor, the Federal Energy Regulatory Commission. (See page A-933 of the Joint Appendix as filed with the Tenth Circuit.)

It was not until after the Jicarilla Apache Tribe commenced this litigation in 1975, in fact, that the Secretary added a *new* legend at the bottom of the monthly statement of account form

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case; Memorandum Opinion filed September 7, 1978 (Mechem, J.) in this case, Jt. App. 68a-69a.

issued to lessees.[8] The new legend added by the Secretary was to the effect that the information being provided to the lessees in the statement of account form was "subject to correction". Such post-litigation addition of this cautionary legend, we submit, was nothing more than a self-serving maneuver by the Secretary, done at the urging and insistence of the Tribe. This conduct by the Secretary only serves to emphasize the prejudicial effect upon the claims being asserted against the defendant producer-lessees which results from the Government-Lessor having regularly issued the statements of account.[9]

The majority decision below appears to clearly impose liabilities upon producer-lessees who acted in reasonable reliance upon the Secretary's administration of oil and gas leases, including the Secretary's issuance of valuation determination as represented in the monthly statements of account given to such lessees. This holding conflicts with the statements of this Court in *Mitchell II, supra,* wherein this Court stated:

> Given the existence of a trust relationship, it naturally follows that the Government should be liable in damages for the breach of its fiduciary duties. It is well established that a trustee is accountable in damages for breaches of trust. *See* Restatement (Second) of Trusts §§ 205-212 (1959); G. Bogert, Law of Trusts and Trustees § 862 (2d ed. 1965); 3 A. Scott, Law of Trusts § 205 (3d ed. 1967). 463 U.S. at 226-27.

The majority *en banc* opinion below, moreover, imposed liability upon the innocent producer-lessees despite the fact that the District Court had expressly concluded that any failure to account

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[8] A photostatic copy of a USGS Form 9-1424 (rev. 12-68) as rendered in 1972 by the United States Department of Interior, Geological Survey to lessees under Indian oil and gas leases is contained in the Annex to this brief at p. 1a, *infra.*

[9] We note, parenthetically, that "dual accounting" also came about only after the litigation had been commenced. See the discussion by Judges Seth, McWilliams, and Barrett in the dissenting *en banc* opinion. Jt. App. 13a, 782 F.2d at 861.

and pay for royalties resulted from "no apparent fault" of the producer-lessees. Jt. App. 127a, 479 F. Supp. 549.[10]

The common law principles referred to by this Court in both *Mitchell II, supra,* and *Nevada, supra,* support the proposition that innocent third party producer-lessees should not be held accountable for a trustee's alleged breaches of fiduciary obligations. *See,* Restatement (Second) of Trusts § 326 (1959) (third parties liable to a beneficiary only if they have notice of a breach and participate in it); see, also, A. Scott, the Law of Trusts §§ 321, 326, 326.1, 326.6 (2d ed. 1956); *International State Bank* v. *Bray,* 87 N.M. 350, 352, 533 P.2d 583, 585 (1975); *Voss Oil Co.* v. *Voss,* 367 P.2d 977, 980 (Wyo. 1962).

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[10] See also the discussion in the memorandum opinion of the District Court filed September 7, 1978. Jt. App. 68a-69a.

CONCLUSION

As is evidenced by the sharply divided decision of the Tenth Circuit below (4–3), this case raises important questions concerning the administration of Indian lands. Because the majority decision below conflicts with the principles announced by the Court in *Mitchell II, supra,* and *Nevada, supra,* the terms of the lease agreements at issue, and settled principles of trust law, certiorari should be granted.

Respectfully submitted,

Original Signed By
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CERTIFICATE OF SERVICE

I hereby certify that I caused a true and correct copy of the foregoing Brief of Amici Curiae In Support of Petitions For Certiorari to be mailed, by placing same in the United States mail, postage prepaid, to the following counsel of record on the 25th day of August, 1986.

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ERNEST J. ALTGELT, III

ANNEX

ANNEX

UNITED STATES
DEPARTMENT OF THE INTERIOR
GEOLOGICAL SURVEY

ISSUING OFFICE: 1
REGIONAL SUPERVISOR
CONSERVATION DIVISION

2002 FEDERAL BUILDING
P. O. BOX 2859
CASPER, WYOMING 82601

STATEMENT OF ACCOUNT

ACCOUNT NO. 35 14-20-258-001348 WYOMING
IND TRIBAL LAND FIELD 713

1

CONTINENTAL OIL CO
DRAWER 1267
PONCA CITY, OK 74601

185

2

JOINT BUSINESS COUNCIL
FT WASHAKIE, WY

4:

REMIT BY CHECK, DRAFT OR MONEY ORDER — NO RECEIPT WILL BE ISSUED

STATEMENT FOR MONTH ENDING 12/31/71				BALANCE FROM THE PREVIOUS STATEMENT		- 0 -	45.00
EXPLANATION				LEASE QUANTITY	LEASE VALUE ROYALTY QUANTITY	UNAPPLIED RENTAL	CHARGES AND PAYMENTS
GAS	ADJ977	512	07/70	140,172.00	21,780.77		3,630.13
GAS	ADJ977	512	07/70	140,172.00CR	21,750.39CR		3,625.07
GAS	ADJ977	512	08/70	155,770.00	24,204.48		4,034.08
GAS	ADJ977	512	08/70	155,770.00CR	24,003.80CR		4,000.63
GAS	977	840	11/71	267,714.00	45,423.84		7,570.64
OIL	977	963	12/71	2,664.47	8,473.03		1,412.17
GAS	977	963	12/71	270,501.00	45,195.15		7,532.53
PAID 11/71 GAS 185 X342 08 01/06/72							38.51
PAID 11/71 GAS 185 X342 08 01/06/72							7,570.66
PAID 11/71 GAS 185 X361 08 01/31/72							7,532.66
					BALANCE	- 0 -	1,457.02

REMIT CHECKS PAYABLE TO "UNITED STATES GEOLOGICAL SURVEY" AND FORWARD TO ISSUING OFFICE ABOVE. ROYALTY REPORTS AND OIL AND GAS PAYMENTS SHALL BE MADE IN ACCORDANCE WITH SPECIFIC INSTRUCTIONS FROM ISSUING OFFICE

LAST ITEM IS YOUR BALANCE

BEST AVAILABLE COPY

MOTION FILED
SEP 13 1986

Nos. 86-219, 86-224, 86-225 and 86-226

In The

Supreme Court of the United States

October Term, 1986

SOUTHERN UNION COMPANY,
SOUTHLAND ROYALTY COMPANY,
EXXON CORPORATION, and
UNICON PRODUCING COMPANY,

Petitioners,

v.

JICARILLA APACHE TRIBE,
DONALD P. HODEL, Secretary of the
United States Department of the Interior,
and STATE OF NEW MEXICO,

Respondents.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

MOTION FOR LEAVE TO FILE BRIEF AMICUS CURIAE AND BRIEF AMICUS CURIAE OF MOUNTAIN STATES LEGAL FOUNDATION IN SUPPORT OF PETITIONERS

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Nos. 86-219, 86-224, 86-225 and 86-226

In The
Supreme Court of the United States
October Term, 1986

SOUTHERN UNION COMPANY,
SOUTHLAND ROYALTY COMPANY,
EXXON CORPORATION, and
UNICON PRODUCING COMPANY,

Petitioners,

v.

JICARILLA APACHE TRIBE,
DONALD P. HODEL, Secretary of the
United States Department of the Interior,
and STATE OF NEW MEXICO,

Respondents.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

MOTION FOR LEAVE TO FILE BRIEF AMICUS CURIAE IN SUPPORT OF PETITIONERS

Mountain States Legal Foundation (MSLF or the Foundation) respectfully moves this Court, pursuant to Rule 42 of the Rules of the United States Supreme Court,

for leave to file the attached brief *amicus curiae* in support of the Petitioners. The consent of the attorneys for the Petitioners Southern Union Company, Southland Royalty Company, Exxon Corporation, and Unicon Producing Company and the consent of the attorneys for Respondents Secretary of the Interior and the State of New Mexico, has been obtained.[1] The consent of the attorney for the Respondent Jicarilla Apache Tribe was requested but refused.

In support of this motion, the Foundation states:

1. MSLF is a nonprofit, membership, public interest law foundation dedicated to bringing before the courts those issues vital to the defense and preservation of individual liberties, private property rights, and the free enterprise system. The Foundation takes a great interest in questions of law having a national scope and especially those that have a direct impact in the Mountain States region, including the State of New Mexico where the instant case arose. Many MSLF members enter into contracts with Indian tribes. If this decision is allowed to stand, their contract interests may also be affected.

2. The issue raised by this case—whether the Secretary's fiduciary duty to Indians can abrogate major tenets of contract law and construction simply because one of the contracting parties is an Indian tribe—has far reaching ramifications for all parties who seek to enter into contracts with Indians. As *amicus curiae,* the Foundation seeks to bring before this Court fundamental policy

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[1]MSLF has filed the written consents of these parties with the Clerk of the Court.

considerations regarding the adverse impacts the Tenth Circuit's decision has on the integrity of contracts that are the cornerstone of the American economic system.

3. These considerations, while directly applicable to the instant case, transcend the specific interests of the parties hereto and thus may not be adequately addressed by the existing parties.

For the foregoing reasons, MSLF respectfully requests that its motion for leave to file the attached brief *amicus curiae* be granted.

Dated this 11th day of September, 1986.

Respectfully submitted,

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BRIEF AMICUS CURIAE OF MOUNTAIN STATES LEGAL FOUNDATION IN SUPPORT OF PETITIONERS

Mountain States Legal Foundation (MSLF or the Foundation) respectfully submits this brief amicus curiae in support of the position of Petitioners in these cases.

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INTEREST OF AMICUS CURIAE

MSLF is a nonprofit, membership, public interest law foundation dedicated to bringing before the courts those issues vital to the defense and preservation of individual liberties, private property rights, and the free enterprise system.

In this case, the Foundation seeks to maintain the viability and integrity of contracts entered into with Indian tribes. Under the Tenth Circuit Court of Appeals decision, contracts with Indian tribes are no longer governed by general principles of contract law and construction. Under the rubric of the government's fiduciary duty to Indians, the Tenth Circuit has held that every contract provision can be reinterpreted at a later date in a manner contrary to the intent and course of performance of the parties, and in defiance of longstanding administrative interpretation of regulations and trade usage.

The uncertainty injected into existing and future contracts with Indian tribes by the Tenth Circuit's ruling can only result in inefficiency and expense to all parties involved and the general public.

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STATEMENT OF THE CASE

Amicus curiae adopts Petitioners' statement of the case in their petitions for writ of certiorari.

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REASONS FOR GRANTING THE WRIT

I. THE TENTH CIRCUIT'S APPLICATION OF THE SECRETARY'S FIDUCIARY DUTY TO REFORM A CONTRACT WITH AN INDIAN TRIBE CONFLICTS WITH OTHER COURTS' DECISIONS CONSTRUING CONTRACTS WITH INDIAN TRIBES IN ACCORDANCE WITH GENERAL PRINCIPLES OF CONTRACT LAW.

By rewriting the lease agreements between Petitioners and the Indian tribe, the lower courts ignored the intent and understanding of the contracting parties when the contract was entered. The contract was revised, over a quarter of a century later, in light of some new interpretation of a royalty regulation based upon the Secretary's fiduciary duty to Indians. Under the Tenth Circuit's novel interpretation, not only can contracts with Indians be unilaterally reinterpreted in favor of the Indian tribe, but the unaware private party can be held retrospectively liable for the cost of the Secretary's perceived breach of trust.

No finding was ever made below that the Secretary's longstanding interpretation of the royalty regulation,[1] generally, or as applied in this case prior to the present litigation, was unreasonable. In fact, royalty calculations based upon the value of the unprocessed wet gas at the wellhead have been uniformly applied and accepted in the industry since this regulation was adopted, regardless of whether an Indian tribe was a party to the lease. As the Tenth Circuit panel found,

> From 1950 to 1979 without exception, and without variation, the Secretary and the USGS had construed the

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[1] 25 C.F.R. § 211.13, J. App. 224a-225a.

> lease provisions and the regulations to require dual accounting not by all lessees, but *only* in instances where the lessee owned the processing plant (or received added money for its products).

J. App. 24a.

The intent of the parties, as evidenced by their course of performance, longstanding administrative interpretation of the regulation, and trade usage should form the basis of interpretation of the leases at issue.[2]

In this case, the lease contracts involved repeated occasions for payment of royalties and opportunity for objection by the United States and the Indian tribe. However, no objection was made for over twenty years. It is, therefore, clear that the parties to the leases had a meeting of the minds as to the meaning of the royalty provision.

In *United States v. Lewiston Lime Co.*, 466 F.2d 1358, 1360 (9th Cir. 1972), the court made clear that the intent of the parties is overriding, even when the contract concerns a lease agreement with an Indian tribe. In that case, after seventeen years of accepting royalties from the lessees without objection under a lease to mine limestone from Indian land, the United States sued to impose a different method of calculating the royalty in order to increase payments to the Indians. The court, finding the roy-

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[2]See Restatement (Second) of Contracts § 202 (1979) (a contract should be construed to reflect the intent of the parties at the time it was formed). *See also* F. Cohen, *Handbook of Federal Indian Law*, 224 n.60 (1982 ed.) (agreements, which directly involve negotiations with Indian tribes, should be construed as the Indians would have understood them).

The intent of the parties to a contract is often best evidenced by their conduct and course of performance over the life of the contract. Any course of performance accepted or acquiesced in without objection is relevant to determine the meaning of the contract provisions. See U.C.C. § 2-208(1) (1978).

alty provision ambiguous, held that the contract was to be interpreted based upon the original intentions of the parties. *Accord, United States v. Wichita Industries, Inc.*, 390 F.Supp. 1154, 1157 (W.D.Okla. 1974) (in interpreting royalty provisions in oil and gas leases on Indian lands, "[c]ourts should strive to ascertain the intent of the parties.")

In another case, additional royalties were denied the Indian lessors because the conduct of the Secretary and the lessee showed a consistent interpretation of the lease as to royalty rights that did not include additional payments. *White Bird v. Eagle-Picher Co.*, 390 F.2d 831 (10th Cir. 1968).

In addition to course of performance, trade usage is also important in interpreting contract provisions. The Tenth Circuit has previously held that parties to a contract are presumed to be aware of well-defined trade usage. *United States v. Stanolind Crude Oil Purchasing Co.*, 113 F.2d 194 (10th Cir. 1940). In that case, the United States had sued to recover additional royalties under an oil and gas lease on Indian land. The court denied recovery holding that, in computing the Indians' royalty interest under existing regulations and an executive order, it would be presumed that the United States knew of the trade usage of deducting a percentage of oil from the royalty calculation to account for impurities, therefore lessees properly deducted three percent from the royalty payment to the Indian tribe. *Id.* at 200.

The Tenth Circuit decision disregards the intent of the parties and ignores other important precepts of contract construction simply because one of the contracting parties is an Indian tribe. Other federal court decisions

have not used the fiduciary duty doctrine to reform contracts made with Indian tribes when to do so runs counter to principles of contract law. Rather, these courts have construed lease contracts with Indian tribes like any other contract. The decision of the Tenth Circuit conflicts with these other courts because it ignores the basic principles of contract law.

II. THE USE OF THE FIDUCIARY DUTY DOCTRINE AS CONCEIVED BY THE TENTH CIRCUIT THREATENS FUTURE REFORMATION OF MANY OTHER CONTRACTS WITH INDIAN TRIBES.

The Tenth Circuit's decision destabilizes the entire field of contract law when one of the contracting parties is an Indian tribe. The ramifications of this case go far beyond the facts and make contracting with Indians an inherently risky proposition.

Rather than facilitate agreements between Indians and private parties, the holding of the Tenth Circuit will only serve to thwart efforts at negotiating such contracts by injecting uncertainty into them. Such a result will be costly and inefficient for everyone involved.

Private parties will be loath to enter into contracts with Indians for fear that the contract will be interpreted at a later date to their detriment, and in a manner they never intended. In addition, private parties will be compelled to require different provisions in contracts with Indians than in contracts with other private parties in order to protect themselves.

There are a multitude of existing contracts with Indian tribes for development of their natural resources, all of which are now open to reformation under the Tenth Circuit's ruling. Indian tribes have also entered into con-

tracts for goods and services which, under the lower court decision, can now be put at issue. Given the uncertain validity of the terms and conditions of these contracts engendered by the Tenth Circuit's decision, private parties face heretofore uncalculated burdens in doing business with Indian tribes. Risks of this nature, especially in light of the amount of retrospective relief afforded in this case, will deter private parties from entering into contracts with Indians. Surely this is not the result intended by Congress in its attempt to promote Indian self-sufficiency and to permit Indians to realize economic benefit from the natural resources on their lands.

CONCLUSION

There is a clear and immediate need for this Court to define a workable standard to apply in interpreting contracts between Indian tribes and private parties. The standard enunciated by the Tenth Circuit replaces the stability and predictability of existing rules of contract law and construction with chaos. The Court should grant the Certiorari Petitions and resolve the confusion that exists.

Dated this 11th day of September, 1986.

Respectfully submitted,

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